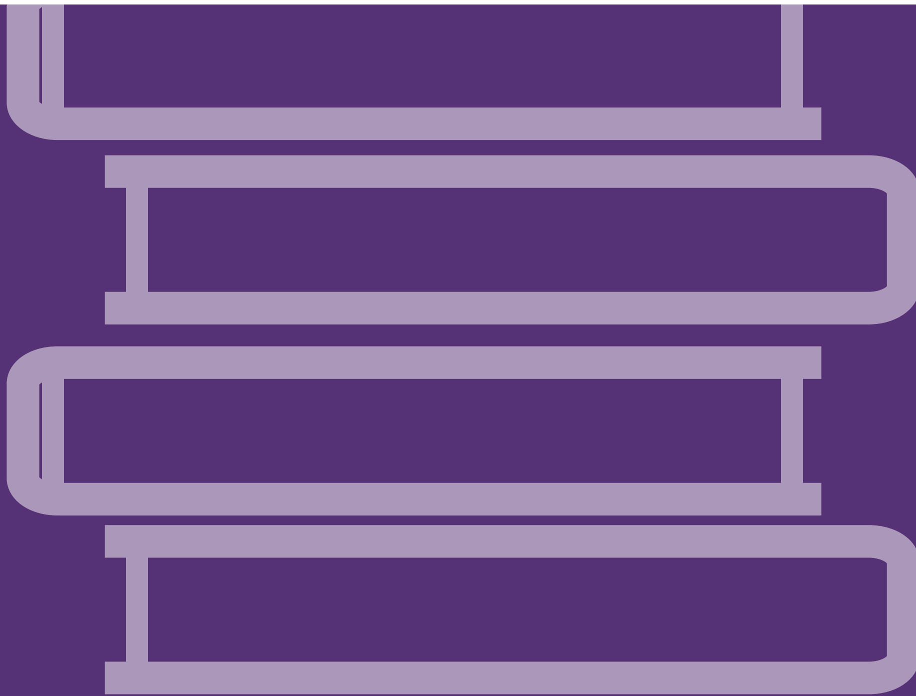
British
Private Equity &
Venture Capital
Association



Technical Bulletin

Keeping you at the forefront of private equity
and venture capital in the UK

May 2017 ////

Contents

Introduction

Welcome to the BVCA Technical Bulletin, a collection of in-depth articles by members of our three technical committees: Taxation; Legal & Accounting; and Regulatory. Our goal is to keep BVCA members informed of the key topics on the committees' agendas, how these impact the private equity and venture capital industry, and how the BVCA and committee members are engaging with policymakers. The Bulletin is published twice a year.

Over the last six months there have been developments on a number of important topics affecting the tax, legal, accounting and regulatory landscape. The three technical committees have continued to monitor these and, when necessary, engage with policymakers in order to shape any emerging regulation. We also strive to keep our members informed of important developments and explain their impact.

The uncertainty surrounding the upcoming Brexit negotiations continues to dominate the BVCA's workload, and this has been further complicated by the calling of the UK general election on 8 June. We expect the Great Repeal Bill and a number of other Brexit related bills to dominate the next parliament. The key priorities for the private equity and venture capital industry and the approach to the Brexit negotiations is covered in the opening article by Gurpreet Manku.

The other major piece of work has been the government's Green Paper on Industrial Strategy. In our response, we suggested ways the government can positively contribute to the UK economy by supporting investment, helping innovative businesses to grow, and ensuring the UK's asset management industry is globally competitive. Other legislation on our agenda include the proposed corporate governance reforms, the patient capital review and changes to partnership law.

The ongoing OECD BEPS process continues to be an area of focus for the Taxation Committee, as well as a number of domestic reforms and consultations. We are still awaiting further clarity on the treaty abuse proposals and the US Treasury approach remains uncertain. The calling of a general election meant that all the major clauses in the Finance Bill were delayed, and there will be further information in future bulletins. In Jenny Wheater's article, she examines how HMRC has increased its focus on legislation designed to influence the behaviour of taxpayers and their advisers.

For the Legal and Accounting Committee, there is now a lot more input required for UK policy making and this is expected to continue throughout the Brexit process. The first article in this section by Amy Mahon, examines a number of areas of law which have either recently changed or will be changing, which impact private equity portfolio companies and fund managers. Corporate governance reforms are addressed in Thomas Laverty's piece, which focusses on the BEIS enquiry and the BVCA's engagement on the green paper.

The competitiveness of the UK private funds industry received a boost in April following the implementation of reforms to UK limited partnership law. We had been in discussions with HMT on these changes since 2013 and the legislative reform order for Private Fund Limited Partnerships was finalised in April. This is the topic covered in Geoff Kittredge's piece and Ed Hall discusses the BEIS review of limited partnership law.

This section concludes with our case law update, drafted by Ed Griffiths, which provides an overview of English court judgements issued in the past six months.

For the Regulatory Committee, the regulation surrounding marketing under AIFMD continues to be an issue. The emphasis had been on passporting and access to investors even before Brexit but more so now, and a review is scheduled for later in 2017. The BVCA also collaborated with Invest Europe on the review of the prudential regime for investment firms.

Amy Mahon
Chair, Legal & Accounting Committee

Mark Baldwin
Chair, Taxation Committee

Tim Lewis
Chair, Regulatory Committee

Gurpreet Manku
Assistant Director General & Director of Policy, BVCA

Whilst the UK remains a member of the EU it is still subject to its laws and continues to implement EU regulation. In the first regulatory article, Louise Dumican gives an update on the European Market Infrastructure Regulation ("EMIR"). MiFID II is addressed in Tim Lewis's article, which provides an update on the new rules being introduced by the FCA. The Fourth Money Laundering Directive is covered in Paul Ellison's article.

To conclude the bulletin, there is a jargon buster prepared by the BVCA policy team and a brief word on the new BVCA website.

Our committee members

The BVCA is immensely grateful for the time, enthusiasm and expertise of members of the technical committees as their work is crucial to our political engagement and advocacy activities.

We would like to thank all members that have served on the technical committees, including those who have recently stepped down, for their considerable contributions. In particular, we would like to thank David Nicolson who stepped down from the Taxation Committee. David was the most recent chair as well as a longstanding committee member, and his extensive experience and sheer dedication has been immensely valuable to us. We would also like to welcome new members to our committees.

	New members on our committees	Members who stepped down
Taxation Committee	**James Pratt** (BDO) **Tony Mancini** (KPMG)	**Adam Frais** (BDO) **David Nicolson** (Bridgepoint)
L&A Committee	**Victoria Sigeti** (Freshfields Bruckhaus Deringer)	**David Higgins** (Freshfields Bruckhaus Deringer)
Regulatory Committee	**Paul Cook** (YFM Equity Partners) **Paul Ellison** (Macfarlanes) **John Morgan** (Pantheon Ventures)	**Fidelis Wangata** (Pantheon Ventures) **Stephen Robinson** (Macfarlanes)

We would also like to extend our thanks to the excellent secretariat at the BVCA who support the work of our three committees so well.

If you have any questions, or would like to get more involved in the work of the committees and their working groups, please feel free to get in touch with any of us.

With best wishes,

Amy Mahon

Chair,
Legal & Accounting Committee

Mark Baldwin

Chair,
Taxation Committee

Tim Lewis

Chair,
Regulatory Committee

Gurpreet Manku

Assistant Director General & Director of Policy, BVCA

Taxation Committee	Legal & Accounting Committee	Regulatory Committee
Mark Baldwin **(Chair)** Macfarlanes	**Amy Mahon** **(Chair)** Clifford Chance	**Tim Lewis** **(Chair)** Travers Smith
Abigayil Chandra Deloitte	**Julie Bradshaw** **(Vice Chair)** Doughty Hanson	**Andrew Lewis** ICG
Alexander Cox Ashurst	**Alastair Richardson** 3i	**Babett Carrier** Cinven
Alexandra Hone ICG	**Ashley Coups** EY	**Christopher Crozier** Permira
Anthony Stewart Clifford Chance	**Duncan Tennant** Permira Advisers	**Ed Kingsbury** Dechert
Clare Copeland	**Ed Griffiths** DLA Piper	**James Smethurst** Freshfields Bruckhaus Deringer
Craig Vickery Exponent PE	**Ed Hall** Goodwin Procter	**John Decesare** 3i
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Fiona Cooper Starwood	**Geoff Bailhache** Blackstone	**Louise Dumican** Carlyle
Gareth Miles Slaughter & May	**Geoff Kittredge** Debevoise	**Mark Howard** KKR
Graham Iversen Greenberg Traurig Maher	**Graham Hislop** Montagu	**Neel Mehta** Mayfair Equity Partners
James Pratt BDO	**Iain Bannatyne** KPMG	**Paul Cook** YFM Equity Partners
Jenny Wheater Linklaters	**John Atherton** Adveq Management	**Paul Ellison** Macfarlanes
Jill Palmer 3i	**John Heard** Abingworth	**Rachel Thompson** Bridgepoint
John Cox KPMG	**Jonathan Wood** Weil	**Simon Powell** Advent International
Jonathan Page PwC	**Richard Mcguire** PwC	**Sheenagh Egan** Livingbridge
Maria Carradice Mayfair Equity Partners	**Robin Bailey** Pantheon Ventures	Secondee: **Sam Bishop** Travers Smith
Matthew Saronson Debevoise	**Sally Roberts** Accel	
Michael McCotter Doughty Hanson	**Stephanie Biggs** Travers Smith	
Paul Cunningham Helios Investment Partners	**Thomas Laverty** Kirkland & Ellis	
Paul Warn EY	**Trudy Cooke** Terra Firma	
Richard Vitou Deloitte	**Victoria Sigeti** Freshfields Bruckhaus Deringer	
Russell Warren Travers Smith	Secondee: **Tamsin Collins** Clifford Chance	
Sarah Priestley Goodwin Procter		
Stephen Pevsner Proskauer		
Tim Hughes PwC		
Tony Mancini KPMG		
William Shaul KPMG		
Secondee: **Jonathan G Hurd** EY		

01.

Brexit update

Gurpreet Manku, BVCA

01. Brexit update

On 29 March, and nine months after the UK voted to leave the EU, the Prime Minister triggered Article 50 in a letter to the President of the European Council. Less than a month later, a UK general election on 8 June was called which means that at the time of writing this update, ministers and officials in the Civil Service are in the pre-election period known as purdah. During this time policy decisions and meetings with officials are postponed until after the election. In practice this will not impact the two-year period over which the UK negotiates its withdrawal from the EU as much of the substance is only expected to be agreed later this year.

Gurpreet Manku
BVCA

This update includes an overview of recent developments and the BVCA work on key Brexit priorities for our members and broader initiatives.

Industry priorities

At this stage, we have seen both the UK and the EU publish high level guidance on the negotiation process. Before commenting on these, it is worth reiterating the key priorities for the venture capital and private equity industry. These were covered in more detail in the November 2016 Bulletin and are:

- **Access to talent:** Being able to attract highly-skilled people and entrepreneurs to the UK, as well as allowing venture capital and private equity fund managers and portfolio companies to find the skilled employees that they need and at suitable speed, is an urgent priority. This includes confirming that EU nationals who are working in the UK already can stay to provide business with the certainty it needs.
- **Continued funding for the UK venture and growth capital funds:** The support of the European Investment Fund ("EIF") as an investor has been crucial to many UK venture capital, growth and mid-market funds[1] which would not have been able to invest in UK businesses without that funding. This level of funding must continue to support UK start-ups and innovative high-growth companies. Further consideration of this and the role of the British Business Bank is covered below.
- **Investor access to UK funds:** The UK private equity and venture capital industry requires and encourages cross-border investment with the rest of the EU ("rEU"). Operations, systems and processes are also intrinsically cross border, and need to be for the industry to be cost effective and function efficiently. Over the past three years (2013-2015), 18 per cent (£6.1bn) of funds raised by the UK industry were from rEU countries. A key priority for our industry is to ensure UK firms still have access to EU investors and vice versa as a loss of access to the European market would substantially impact the ability of the UK industry to raise funds and could reduce the amount of investment available to businesses in both the UK and Europe. As a minimum, European National Private Placement Regimes must remain open to UK firms. This would be alongside third country access for UK firms through a new relationship with the rEU.
- **Transitional arrangements:** There is expected to be a period of time between the day the UK leaves the EU and the agreement of a bilateral trade deal with the rEU. Therefore, a sensible transitional arrangement between the UK and the rEU needs to be in place and agreed early on in the negotiation process to avoid cliff edge scenarios on Brexit day. The BVCA submitted a response to the Treasury Select Committee enquiry on this area and this also explained the different ways of marketing to investors in the rEU.

[1] Between 2011 and 2015 the EIF directly invested €2.3bn of investment into the UK venture capital and growth funds industry.

- **Other matters:**
  - A number of BVCA members have firms that are regulated under MiFID and we are therefore reviewing the impact of Brexit on these firms.
  - In terms of tax, all EU member states are party to two European Directives which remove withholding tax on dividends, interest and royalties in most cases – the Directive on parent companies and subsidiaries in different member states (commonly known as the EU Parent-Subsidiary Directive) and the Interest and Royalties Directive. If access to these directives is lost following the UK's exit from the EU, the use of UK holding companies for investments within the EU may be impaired due to potential for tax leakage on dividends and interest paid by an EU subsidiary to its UK parent. While it should still be possible for the relevant double tax treaty to apply, the UK's treaties are not always as beneficial as the directives, as they do not always provide for nil withholding tax on dividends and interest.
  - We are also assessing the impact on portfolio companies. Given the wide range of sectors in which our members invest, our starting point is to establish private equity and venture capital-specific issues at a transactional level and then other ongoing matters that affect all portfolio companies, such as laws on data protection and competition.

The UK's position

Earlier this year the government published a white paper on the principles that would guide the negotiations as it seeks a new relationship with the EU. These are:

- Providing certainty and clarity;
- Taking control of our own laws;
- Strengthening the Union;
- Protecting our strong historic ties with Ireland and maintaining the Common Travel Area;
- Controlling immigration;
- Securing rights for EU nationals in the UK and UK nationals in the EU;
- Protecting workers' rights;
- Ensuring free trade with European markets;
- Securing new trade agreements with other countries;
- Ensuring the United Kingdom remains the best place for science and innovation;
- Cooperating in the fight against crime and terrorism; and
- Delivering a smooth, orderly exit from the EU.

The white paper and the notification letter noted the UK's willingness to establish as early as possible in the negotiations the status of EU nationals currently in the UK and of UK nationals abroad. The white paper recommits the government to seek "the freest possible trade" in financial services as part of a future UK-EU trade deal and the letter notes the UK's desire for an "bold and ambitious free trade agreement". The white paper also acknowledges the need for implementation periods to avoid "a disruptive cliff edge" and makes it clear that any transitional status needs to have a fixed time period. From a venture capital and private equity perspective this is positive, however we will need to carefully scrutinise the detailed proposals.

The European response

On 29 April the European Council adopted guidelines that define the framework for negotiations and sets out the EU's position and principles it will pursue. The next step in the process was for Council to approve the proposal and negotiating directives recommended by the European Commission to open the negotiations and nominate the Commission as the EU's negotiator. This was approved on 22 May. Both the guidelines and negotiating directives noted the resolution adopted by European Parliament on 5 April. In summary, these documents cover similar ground including the need to preserve the EU's interests and those of its citizens, businesses and members states. The negotiating directives provide a little more detail on the guidelines and both of these documents will be updated throughout the negotiation process.

The guidelines state that there will be a phased approach to negotiations giving priority to an orderly withdrawal before discussions on the preliminary framework for a future relationship and any form of transitional arrangements. The UK had hoped for these discussions to take place concurrently. The EU also notes that the negotiations will be conducted transparently and as a single package, i.e. nothing is agreed until everything is agreed. Therefore there will be a period of uncertainty even if an agreement on EU and UK nationals and transitional arrangements is reached early on. The negotiating directives only cover areas relevant to the withdrawal agreement being: citizens' rights; the financial settlement; arrangements regarding goods placed on the market and ongoing procedures based on EU law; arrangements relating to other administrative issues; and governance of the agreement. Therefore matters such as transitional arrangements will be covered at a later date once progress has been made on the future relationship.

The guidelines note the free trade agreement should be "balanced, ambitious and wide-ranging", however the EU expects a "level playing field, notably in terms of competition and state aid, and in this regard encompass safeguards against unfair competitive advantages through, inter alia, tax, social, environmental and regulatory measures and practices." Although the UK will start in the same position as the EU on regulatory and tax policy, changes to this over time will depend on how the negotiations develop.

Government publications and consultations

The Great Repeal Bill

In April, the government published a white paper and guidance for businesses on the Great Repeal Bill. The Bill will repeal the European Communities Act 1972 and convert EU law into domestic law when we leave the EU to help provide for a smooth and orderly exit. The white paper sets out the steps this will entail, including the creation of powers for the government to make secondary legislation, as well as the impact on the devolution settlements, Crown Dependencies and Overseas Territories. We expect there to be an additional 10 to 15 bills alongside the Great Repeal Bill including one relating to migration.

From a BVCA perspective, we will need to engage with government during this process as there is a significant amount of EU legislation, particularly regulation for fund managers, that the UK will review as part of this process. This is because it will not be able to simply "copy and paste" EU law into the UK statute and will have to make amendments where for example there are references to "EU law", the involvement of an EU institution and information sharing with EU institutions as the UK will become a third country. It will also make changes to reflect the content of the withdrawal agreement under Article 50.

To make these changes, the government is proposing to use secondary legislation and requesting relatively wide delegated powers to do this, as it is impractical to know how every law will be amended at this stage. They estimate that between 800 to 1000 statutory instruments will be needed as part of this process. The Great Repeal Bill will begin its passage through Parliament in the coming months, running alongside the UK's negotiations with the EU.

Industrial Strategy and Patient Capital Review

The government has consulted on the content of its Industrial Strategy green paper. This sets out ten key ‘pillars’ of policy spanning research and innovation, infrastructure, business investment, skills and more, with the intention of building a better functioning economy in the UK. The Patient Capital Review – conducted by HM Treasury with the assistance of a practitioner-led advisory panel chaired by Sir Damon Buffini – is referred to in the green paper, and will investigate barriers to long-term finance for firms looking to scale up as well as the tax advantaged venture capital schemes. The Industrial Strategy consultation closed on 17 April, and a further consultation linked to the Patient Capital Review is expected to launch after the general election.

In a detailed response to the green paper, the BVCA notes that Brexit will lead to a period of uncertainty for our members and the businesses in which they invest. We have suggested ways the government can positively contribute to the UK economy by supporting investment, helping innovative businesses to grow, and ensuring the UK’s asset management industry is globally competitive. We believe the British Business Bank should play a vital role in drawing in private capital through increased investment in venture capital funds. We welcomed the additional funding committed by the government in the Autumn Statement 2016, however, this level of funding must increase to match that currently provided by the EIF.

Member briefings

To keep our members updated over what will be an extended period of uncertainty and potential change, we will continue with our breakfast series and supplement this with political analysis offered by BVCA publications, alongside further information on tax, legal and regulatory aspects through our monthly Technical Updates. Further detail on the BVCA’s priorities, political analysis and representations can be found on the Brexit portal.

To coincide with the triggering of Article 50, the BVCA launched a Brexit Bulletin, a monthly online briefing on key policy and political matters. The Brexit Primer is also available on our website, which includes information on the upcoming negotiation, relevant legislative developments in the UK, and the institutions that will be involved.

For political analysis and commentary from our Director General in the run up to the election, please sign up to his weekly email, BVCA Insight.

02.

Failure to prevent tax evasion

Jenny Wheater, Linklaters

02. Failure to prevent tax evasion

Jenny Wheater
Linklaters

Introduction

In recent years, HMRC has increased its focus on legislation designed to influence the behaviour of taxpayers and their advisers. In contrast to what might be termed conventional "revenue raising" legislation which imposes additional requirements to actually pay tax, this type of legislation is designed to encourage taxpayers to take courses of action which result in a greater yield for the exchequer, notwithstanding that they may have a choice not to do so. The first example of this was the disclosure of tax avoidance schemes ("DOTAS") regime, which has expanded significantly since its inception. A return including a reference number under DOTAS is not calculated any differently for tax purposes. However, many taxpayers are aware that the very reference number itself will not endear them to HMRC and may trigger an enquiry or other undesirable consequence. If the result is that such taxpayers do not enter into potentially tax saving arrangements simply to avoid the DOTAS reference, HMRC benefits, without actually imposing a specific tax charge.

HMRC have regarded DOTAS as a successful regime and the same concept of influence can now be found in other areas. The most recent of these is the new corporate offence of failure to prevent tax evasion, legislation which owes much of its wording to the Bribery Act.

The new offences

The new offence is contained in what is now the Criminal Finances Act 2017 and is, in reality, two separate offences. The first is the offence of failure to prevent the facilitation of UK tax evasion (the "Domestic Offence"). The second is the offence of failure to prevent facilitation of foreign tax evasion (the "Foreign Offence"). However, they have some key features in common. In each case, a body corporate or a partnership (referred to as a "relevant body"), whether established for business or non-business purposes, may be prosecuted for failure to prevent the facilitation of tax evasion if:

- a person ("T") evades tax;
- an associate ("A") of the relevant body criminally facilitates that evasion while acting in the capacity of an associate of the relevant body; and
- the relevant body is unable to show they had in place "reasonable prevention procedures" (or that it wasn't reasonable for prevention procedures to be in place).

The offences are both strict liability offences and thus require no knowledge or intention. T need not have been prosecuted for evasion and A need not have been prosecuted for criminal facilitation. T (or A) may in fact have made a disclosure of the evasion (or criminal facilitation) in order to secure immunity from prosecution or similar.

A person is an "associate" of the relevant body if the person "performs services for or on behalf of" that body (for example, as an employee, agent or subcontractor). The substance of the relationship will be considered, not just the form. A relevant body will not, however, commit the offence if the associate commits the offence of facilitation on a personal basis – the action must be in their capacity of an associate of the relevant body. The concept of a person who "performs services for or on behalf of" the organisation is intended to be broad in scope, to embrace the whole range of persons who might be capable of facilitating tax evasion whilst acting on behalf of the relevant body. This is important in considering the potential scope of the offence and addressing reasonable prevention procedures discussed below.

The Domestic Offence can be committed by a relevant body irrespective of where they are established or carry on business, and whether or not any part of the criminal facilitation took place in the UK. In fact, wholly non-UK conduct by a non-UK entity can be included, if it is directed at the evasion of UK tax. In such cases, the government still considers that the new offence can be tried by the courts of the UK.

The Foreign Offence can only be committed where:

- the relevant body is established in the UK, or carries on any part of their business in the UK (for example, through a branch);
- any part of the criminal facilitation took place in the UK.

Once again, this gives the law a broad extra-territorial scope: a body corporate may fall within scope and be capable of committing the Foreign Offence merely by virtue of having a UK branch, even if that branch is not itself involved in the facilitation or the evasion.

For the Domestic Offence, a UK tax evasion offence is the common law offence of cheating the public revenue and an offence in any part of the United Kingdom consisting of being knowingly involved in, or taking steps with a view to, the fraudulent evasion of tax. In the case of the Foreign Offence a foreign tax evasion offence has two elements. First, it must be criminal offence under the law of the foreign territory relating to tax imposed under the law of that country, and second, it must involve conduct which would be regarded by the UK Courts as an offence of being knowingly concerned in, or taking steps with a view to, the fraudulent evasion of tax (if it had occurred in the UK).

Facilitation, as anticipated, is subject to a wide interpretation. The person must do an act anticipating that it will assist another person to evade UK tax. Examples in the draft HMRC guidance (the "Guidance") of activities potentially amounting to facilitation (if conducted with the necessary intention to assist the evader), include:

- Delivery and maintenance of infrastructure - for example, trust and company formation and setting up and maintaining bank accounts.
- Financial assistance – helping an evader move money around, providing banking services.
- Acting as a broker or conduit – i.e. arranging access to others in the supply chain.
- Providing planning advice.

It is a complete defence to both of the offences if the relevant body can prove that, when the tax evasion facilitation offence was committed, either (a) the relevant body had in place reasonable prevention procedures; or (b) in all the circumstances it was not reasonable to expect the relevant body to have any prevention procedures in place.

Prevention procedures are those designed to prevent associates from committing tax evasion facilitation offences. As with the Bribery Act, the Guidance states that the formulation of measures to prevent facilitation should be informed by the following six principles:

- Risk Assessment;
- Proportionality of risk-based prevention procedures;
- Top level commitment;
- Due diligence;
- Communication (including training); and
- Monitoring and review.

The Guidance recognises that procedures may leverage existing controls. However, the appropriateness of controls will need to be informed by a considered risk assessment, and simply adding "and tax evasion" to a long list of diverse prohibited activities under existing ethics policies is not expected to be sufficient.

Unlimited fines can be imposed upon conviction and orders for confiscation of assets may also be made. In order to encourage self-reporting by relevant bodies, Deferred Prosecution Agreements ("DPAs") will also be an available tool for prosecutors. DPAs, which are a mechanism for resolving certain types of offending by corporate entities, involve charges being laid but the prosecution being suspended for a specified period provided certain agreed conditions are met.

Application to private equity

The question of how this legislation applies to the private equity fund industry is highly dependent upon the private equity house involved but a number of key areas can be identified as requiring general attention. Crucially, private equity houses need to consider how these new rules apply not only to them directly, but also to other entities within the structure and to their portfolio companies. Portfolio companies themselves need to consider the rules on a separate basis but the interaction between the private equity house and the portfolio company results in the potential for some ambiguity and areas of risk. For example, a director of a portfolio company who is an appointee of the private equity house arguably has a dual potential capacity as an “associate”. Clearly they are a director of the portfolio company but they may also be acting as an associate of the private equity house in relation to their director activities. Thus, reasonable prevention procedures may need to consider this aspect of the role of employees and other possible “associates”.

The breadth of the term “associate” and its extension to those performing services for an entity is also something private equity houses will need to consider very carefully. For example, if a portfolio company engages a firm of advisers which has a more aggressive approach to tax planning than the private equity house might think appropriate, there is a danger that the portfolio company could be regarded as committing the offence through the activities of such adviser if they e.g. advise executives of the portfolio company to conduct their affairs so as to engage in tax evasion. Even non-tax advisers who recommend a particular firm or individual to assist in possibly dubious tax arrangements, could be regarded as acting in their capacity as associate of the portfolio company and facilitating tax evasion. This type of potential scenario results in the need for private equity houses to review with their portfolio companies who their advisers and other contractors are and what their remit is. The category of service providers as associates has the potential to create situations in which the portfolio company may be guilty of an offence in circumstances concerning which the private equity house was wholly unaware.

International issues may also require careful review. It is fair to say that most UK private equity houses have some kind of international activity or presence and this, again, could present issues. If an individual employee of a private equity house is also a board member or employee of e.g. the Luxembourg General Partner of a fund, they could be considered to be acting in that capacity in certain circumstances and, given the breadth of the Domestic Offence, any activity in Luxembourg by an associate of the Luxembourg GP might still be subject to the new rules. Thus, reasonable prevention procedures need to take this into account and may need to extend to the GP itself.

The concept of what amounts to “reasonable” in terms of prevention procedures will require some internal analysis and this will need to be considered on a case-by-case basis. However, all private equity houses will need to approach with care to ensure that they have performed appropriate reviews as to their position and what they are required to do in order to secure protection from potential criminal liability.

Timing

Originally, relevant bodies were required to have their prevention procedures in place by September when the legislation was due to come into effect. However, the upcoming general election may have served to alter this.

In an accelerated progression, the Criminal Finances Bill passed its final stage in the Parliamentary process, as the House of Commons considered the amendments that were introduced in the House of Lords the day before. The Bill then received royal assent on 27 April 2017, thus becoming the Criminal Finances Act 2017. However, although the Act has now become law, key aspects such as the elements relating to failure to prevent tax evasion require a separate commencement order before coming into force. It is not yet clear when this will happen. There has been some suggestion that it could be as early as September or October 2017, but whether or not that is the case, HMRC has made it clear that relevant bodies cannot wait until the Act comes into force before taking action to prepare for the new corporate tax offence.

To help members get to grips with their responsibilities in this area the BVCA will be arranging a series of workshops before the Summer break. We are also arranging to meet HMRC to discuss industry-specific issues before the Summer and will flag up any helpful thoughts or guidance to emerge from that process. But, given the likely timetable, members need to start work on this legislation now, both at the level of their own businesses and at portfolio company level. A first step would be to identify risk areas, where an associate could get involved in facilitating tax evasion, and introduce or modify procedures to try to stop that happening. The implications, in terms of the house's reputation as well as the new rules, are too serious not to put appropriate, tailored processes in place.

03.

Portfolio company matters

Amy Mahon, Clifford Chance
Tamsin Collins, Clifford Chance

03. Portfolio company matters

This article examines a number of areas of law which have either recently changed or will be changing, which impact private equity portfolio companies and fund managers. These are the General Data Protection Regulation which will come into force in May 2018 and the Gender Pay Gap Reporting Regulations and Reporting on Payment Practices and Performance Regulations which both came into force on 6 April 2017.

Amy Mahon
Clifford Chance

Tamsin Collins
Clifford Chance

1. General Data Protection Regulation

Overview

The General Data Protection Regulation (2016/679) ("GDPR") will take direct effect on 25 May 2018 repealing the Data Protection Directive (95/46/EC), which was implemented in the UK by the Data Protection Act 1998.

All businesses in the European Union must be fully compliant with the GDPR by 25 May 2018. Time to prepare is short and, although data protection authorities may act leniently in the early days of the new regime, there is no formal transitional relief to protect existing processing and practices. Therefore both fund managers and private equity portfolio companies should begin preparations now.

Key changes

The basic principles of data protection law remain largely unchanged: fairness, legitimacy, proportionality, security and restrictions on international data transfer. Fund managers and portfolio companies should remember that personal data should not be processed other than where the conditions of transparency, legitimate purpose and proportionality are met.

However, the GDPR introduces new concepts and approaches which will result in most businesses needing to perform a root and branch review of data processing. There is a strong emphasis in the new regime on "accountability" – not just acting fairly and reasonably in the processing of personal data, but having in place a data privacy superstructure designed to ensure, monitor and record compliance.

In particular, the GDPR introduces significant changes in relation to consent, data protection impact assessments and the appointment of data protection officers. Significant new fines are also imposed in the event of a breach. We therefore recommend that fund managers and portfolio companies conduct a review of their data processing procedures and, in the case of portfolio companies, investor directors or fund managers should check this is taking place.

Expanded territorial scope

The GDPR will significantly extend the application of the EU data protection regime, catching GPs and fund managers outside the EEA.

The GDPR, like the current directive, will apply to data controllers (the person who determines the purposes and manner in which personal data is processed) established in the EU, but it will also apply to data processors (a person who processes personal data on behalf of the data controller) and to organisations outside the EU which offer goods or services to EU data subjects or monitor their behaviour.

The GDPR also asserts extraterritorial effect. Broadly, the current data privacy regime applies to processing where the controller and processing activity has a European nexus (e.g. where the controller is established in the EEA or uses equipment in the EEA to carry out the processing activities). The new rules will also apply to processing entirely outside of the EEA (i.e. if such processing is carried out in order to offer goods and services to, or monitor the behaviour of, individuals within the EEA).

"One-Stop-Shop"

The GDPR introduces a consistency mechanism regarding supervision and enforcement of its requirements. This is the so-called "one-stop-shop".

Broadly, the one-stop-shop provides for legal entities within the GDPR's scope established in more than one member state to be regulated by a single lead regulator. The lead authority will be required to coordinate with other local regulators as relevant to the supervision of the relevant regulated legal entity.

The lead regulator will be the regulator in the member state in which the legal entity has its "main establishment". The test for "establishment" is broad. In practice, establishment will usually be ascertained by reference to the relevant entities main administrative location in the EU, unless significant decisions about data processing take place in a different member state.

Rights for data subjects

Obligations owed to data subjects are enhanced by the GDPR. These rights include explaining the basis on which the processing (and any international transfer outside the EEA) is justified, the length of time for which the data will be retained and rights to lodge complaints with the data protection authority.

Consent

Subtle but important changes are made to the requirements for effective consent. Data controllers will be required to demonstrate that a data subject's consent has been obtained, and that the consent is "unambiguous".

The existing practices for obtaining consent therefore need to be reviewed to ensure businesses can demonstrate such consent has been obtained. The consent of a data subject may also always be withdrawn (which is not the current position under UK law) and parental approval will be required for processing children's data.

Data portability

A new limited right for data subjects to request (i) the return of their data to them, or (ii) that their data is passed on to a new replacement data controller has been introduced. The data will need to be transferred in a commonly used, "machine-readable" format. This is the so-called "data portability" right. The data portability right is principally aimed at social media and similar online contexts and businesses in these areas will already be working to address data portability issues in their GDPR implementation strategies.

Recent EU guidance notes that the GDPR does not establish a general right to data portability where the processing of personal data is not based on consent or contract. Fund managers and portfolio companies should therefore consider the circumstances in which the portability right may be used against their respective businesses. If portability would not be feasible or appropriate, consideration should be given to how the right can be avoided (e.g. by relying on "legitimate interests" rather than "consent" to justify processing).

Right to be forgotten

The GDPR does not add much to the existing "right to be forgotten", where an individual can require a data controller to erase their personal data in limited circumstances. It codifies existing EU law. The right will not arise as long as the controller has a legitimate reason to continue processing the data, and once that legitimate reason has expired the controller should in principle delete or anonymise the data anyway, irrespective of the exercise of the right.

Data protection impact assessments

Businesses will be required to carry out data protection impact assessments before carrying out any data processing which involves new technology which is likely to be of high risk to data subjects. Where such assessment deems that the data processing would result in a high risk to individuals, the business must consult with the national data protection authority before any data processing takes place. Non-compliance with the data protection impact assessment requirements can lead to fines imposed by the competent regulator.

The GDPR takes a risk-based approach to compliance. So a data protection impact assessment will not be required in every case. However the scope of this requirement is not yet clear. In practice, at least basic assessments will be needed of all processing arrangements (i.e. to ensure they are GDPR-compliant and determine whether full data protection impact assessments are required).

Record keeping and data protection officers

The GDPR requires businesses to maintain detailed documentation recording their data processing activities. These obligations do not apply to organisations employing fewer than 250 people, other than in certain limited scenarios (e.g. where the processing activities are likely to result in a high risk to individuals or the processing includes sensitive personal data). Therefore this will be relevant to many portfolio companies, but most fund managers will not be caught by the employee threshold. However fund managers and portfolio companies need to remain compliant with the existing data protection legislation, for example when fund managers receive personal data as a result of AML checks they should ensure there is a legitimate interest in obtaining such information and that the information is proportionate.

Companies processing sensitive data on a large scale or whose core activities require regular monitoring of data subjects on large scale will need to appoint a data protection officer. Such data protection officers must have applicable expert knowledge and be able to perform their duties and tasks in an independent manner, which may prove challenging for smaller businesses.

Breach

There is no general "security breach notification" concept under the existing EU data privacy rules. Two new obligations are introduced by the GDPR in the event of a breach.

Firstly, controllers must report all security breaches to the relevant regulator without undue delay, and where feasible, within 72 hours of the controller becoming aware. Secondly, if the breach would likely result in a "high risk" to the "rights and freedoms" of the data subject, the controller must inform the affected data subjects. Processors must also inform their controllers when they become aware of security breaches without undue delay.

A rapid response to each data security breach will be required. Portfolio companies will therefore need to develop a plan enabling them to respond quickly to a data breach. If any technology is outsourced, portfolio companies should consider (i) whether (and, if so, when) they would receive notification of any breach; and (ii) building security breach notification obligations into their contractual framework and security breach readiness strategy.

Enhanced sanctions and remedies for breach

The GDPR substantially increases the risks associated with failure to comply with the EU data privacy regime by increasing the potential sanctions for breach. Potential sanctions fall into four categories: (i) administrative fines; (ii) civil sanctions; (iii) regulatory action; and (iv) criminal penalties.

Currently fines under national law vary and are fairly low, for example in the UK the maximum fine is £500,000. The GDPR increases the fines the competent data protection authority will be able to impose to: (i) up to 4 per cent of global turnover or €20mn (whichever is greater for infringements such as breach of international data transfer provisions), or (ii) up to 2 per cent of global turnover or €10mn (whichever is greater for more minor infringements).

Previously under the Data Protection Directive, statutory obligations were only imposed on data controllers, not data processors. Under the GDPR statutory obligations are imposed on both data controllers and data processors and both will be subject to fines.

The GDPR also gives data subjects the right to bring civil claims for compensation for damage or distress suffered as a result of breaches. From a regulatory perspective, data protection authorities will (i) have clear audit rights (only patchily available under the Directive), and (ii) as under the Directive, will have various powers to compel compliance with the GDPR. Member states will remain free to impose criminal penalties for breach.

Brexit

The GDPR will almost certainly take effect before the UK leaves the EU, which is unlikely to be before March 2019. The government has made it clear that it will do nothing to step back from the GDPR. UK businesses will therefore need to comply with the GDPR in full, at least during the period between May 2018 and Brexit.

Although UK law post-Brexit is likely to be closely based on the GDPR, this does not mean that Brexit will be unproblematic from a data privacy standpoint. The post-Brexit UK may be regarded by the EU as "inadequate" for data transfer purposes until the European Commission determines that UK law ensures an adequate level of protection for EU personal data. Such an "adequacy" decision is not guaranteed.

Unless a transitional or permanent solution to these problems is found through Brexit negotiations, businesses will need to find alternative means to justify future data sharing between the EU and the UK (e.g. standard form data transfer agreements). As such, both fund managers and private equity portfolio companies should take Brexit into account in assessing their international data transfer strategies.

2. New Gender Pay Gap Reporting Regulations

Overview

The Equality Act 2010 (Gender Pay Gap Information) Regulations 2017 (“GPG Regulations”) that implement the new gender pay gap reporting regime came into force on 6 April 2017.

Key aspects of the new regime are as follows:

- The first Gender Pay Gap Reports (“GPG Reports”) must be published on or before 4 April 2018 based on a snapshot of pay data on 5 April 2017.
- Employers in Great Britain (and potentially some employers outside Great Britain) with at least 250 employees will be required to publish information on the difference between the mean and median hourly pay of male and female full-pay relevant employees.
- GPG Reports must also publish how many men and women appear in each quartile of pay distribution.
- Employers will also be required to separately detail the differences between the mean and median bonuses to women and men in the 12 month reference period.
- The GPG report must be published every year on a searchable website accessible by employees and the public.
- The government must be separately notified of compliance by uploading the relevant information to a government sponsored website.

Who is caught?

Initially only private sector employers in Great Britain with 250 or more employees will be subject to the new gender pay gap reporting regime, however, the government will review the position after five years to determine whether other employers should be brought in scope. This means many PE portfolio companies will be caught. Note that the GPG Regulations do not have a territorial definition, so potentially non-UK employers could be caught in respect of their UK employees.

The reporting obligation is by legal entity only. Each qualifying employer within a group will have to produce an individual GPG Report rather than data being aggregated across the group.

A separate but similar regime applies to public sector employers which came into effect on 31 March 2017.

Who is an employee?

An employee for the purposes of the GPG Regulations is an individual who works under a contract of employment, apprenticeship or a contract personally to do work which potentially catches self employed contractors. Employees based outside the UK would also appear to be caught although the government and ACAS consider that only employees with a stronger connection to Great Britain and English employment law would come within the scope of the GPG Regulations. ACAS guidance suggests indications than an employee has a stronger connection and should be included in the GPG report include having a contract subject to British legislation, his home in Great Britain and UK tax legislation applicable to his employment.

LLP partners are excluded from the categories of employee whose data must feature in the GPG Report; therefore, whilst fund managers and advisers will be caught, partner pay will not need to be disclosed. However, they do count towards the 250 employee trigger threshold. LLPs who employ more than 250 employees will be caught by the new regime. Where employee information is required to be disclosed the information should include ordinary pay, bonuses and carried interest.

Consequences of non-compliance

The GPG Regulations do not impose civil or criminal penalties in the event of non-compliance, however the government will keep the position under review. Failure to comply with the regulations would be an unlawful act for the purposes of the Equality Act 2010 in relation to which the Equality and Human Rights Commission could, in principle, bring enforcement action.

3. Reporting on Payment Practices and Performance Regulations 2017

Overview

The Reporting on Payment Practices and Performance Regulations 2017 and the Limited Liability Partnership (Reporting on Payment Practices and Performance) Regulations 2017 came into force on 6 April 2017. They impose a requirement on the UK's largest companies and LLPs to publish information about their payment practices and performance on a half-yearly basis. The information must be published on a government website available to the public.

Who needs to comply?

The reporting obligations apply to (i) companies and LLPs (other than parent companies or parent LLPs) and (ii) parent companies and parent LLPs.

Companies and LLPs (other than parent companies or parent LLPs) which, based on their last two balance sheet dates, exceed two or all of the thresholds for qualifying as a medium-sized company as set out in section 465(3) of the Companies Act 2006 are subject to the reporting obligations. As at the current date, these thresholds are:

- Over £36mn annual turnover;
- Over £18mn balance sheet turnover; and
- More than 250 employees.

Therefore this will only apply to larger portfolio companies. The obligations apply to companies formed under the Companies Act 2006 therefore overseas companies are not required to report. In addition, the obligations only apply to LLPs registered under the Limited Liability Partnerships Act 2000.

Companies and LLPs will not be "qualifying companies" in their first financial year. The information to be reported should be prepared on an individual company or LLP basis, not at group level.

A company or LLP which has one or more subsidiary undertakings (as defined in s1162 Companies Act 2006) is a parent company or parent LLP. It will therefore be necessary to conduct an analysis of the group structure using the subsidiary undertaking test to identify relevant parent entities.

A parent company or parent LLP will be required to prepare an individual report only if both the parent company or parent LLP and the group exceed the relevant size thresholds based on their last two balance sheet dates. Accordingly, in order to determine whether it meets the reporting requirements the parent company or parent LLP must first determine whether it qualifies as an individual entity, exceeding two or all of the thresholds described above. If this test is satisfied then the parent company or parent LLP must determine whether the group headed by that parent company or parent LLP exceeds two or all of the following thresholds:

- An aggregate turnover of £43.2mn gross or £36mn net;
- An aggregate balance sheet total of £21.6mn gross or £18mn net; and
- More than 250 employees.

If the parent does not meet the individual threshold it will not need to report on its own payment practice and performance. If it meets the individual threshold and its group satisfies the group thresholds, then the parent must report on its own payment practices and performance. The parent's report must be prepared on an individual basis and not an aggregated group basis.

Information to be reported on

Companies and LLPs must publish information about their payment practices and performance in relation to "qualifying contracts" for each reporting period in the financial year. A "qualifying contract" is one which (i) is between two or more businesses, (ii) has a significant connection with the UK and (iii) is for goods, services or intangible assets. Financial services contracts are not "qualifying contracts". The definition of financial services contracts includes the asset management and private equity sector so, for example, limited partnership arrangements would not be caught.

The report must include the following:

- Narrative descriptions on standard payment terms and the process for resolving disputes over payment;
- Statistics on matters such as the average number of days taken to make payments and the percentage of payments which were not paid within 30 days or less, 31-61 days and over 60 days during the reporting period; and
- Statements on matters such as the offering of e-invoicing and availability of supply chain finance.

The report must be published on the government website within 30 days after the end of the relevant reporting period.

Consequences of non-compliance

It is a criminal offence by the business, and each director of the company or designated member of the LLP, if the company or LLP fails to publish a report containing the necessary information within the specified filing period. It is also a criminal offence to publish false, misleading or deceptive information. These offences are punishable on summary conviction by a fine.

04.

Corporate Governance Reform

Thomas Laverty, Kirkland & Ellis

04. Corporate Governance Reform

Thomas Laverty
Kirkland & Ellis

On 16 September 2016, the Business, Innovation and Skills (now Business, Energy and Industrial Strategy) ("BEIS") House of Commons Select Committee launched an inquiry on corporate governance, focusing on executive pay, directors' duties, and the composition of boardrooms, including worker representation and gender balance in executive positions.

The inquiry followed the failings highlighted by the Select Committee's inquiries into BHS and Sports Direct, and the Prime Minister's commitments to overhaul corporate governance.

On 29 November 2016, BEIS published a Green Paper on corporate governance reform focused on enhancing the current framework through the following three specific aspects of corporate governance: (i) executive pay, (ii) employee, customer and wider stakeholder voice, and (iii) corporate governance in large privately-held businesses. The Green Paper also invited suggestions on other themes, ideas or proposals which could strengthen the UK's corporate governance framework.On 5 April 2017, the Select Committee published its report on the inquiry.

This article explains the BVCA's engagement in the consultation process and summarises what we consider to be the key points of the inquiry and its outcome for the private equity and venture capital ("PE/VC") community.

BVCA Engagement

The proposals in the Green Paper aimed at strengthening the employee, customer and wider stakeholder voice, and corporate governance in large privately-held businesses were clearly of relevance to BVCA members and PE/VC in the UK more generally.

Accordingly, representatives of the BVCA met with representatives of a number of the consultation's stakeholders, including BEIS, HM Treasury and the Financial Reporting Council, to provide background information about the PE/VC industry and investment model, its positive impact on the UK economy, and the good corporate governance practices in place and publications developed by the industry on professional standards and responsible investment.

The BVCA then submitted a formal response to the Green Paper which reiterated those factors and emphasised the following points:

- Recognition that there have been examples of corporate failures where it appears that corporate governance has not worked in the way it should. As well as impacting on the reputation of UK businesses, this has led to an erosion of public trust which now needs to be restored. It is however important to remember that there are also many examples of well-run companies where there are robust and effective governance structures in place which have helped create long-term value.
- Any reform in this area must be both proportionate and balanced so that, whilst helping prevent corporate failures, reform designed to deal with the behaviour of a minority of companies does not discourage investment in the UK. Nor should it disproportionately impact on the competitiveness of the UK as a place to locate and to do business.
- Given (i) the close relationship between PE/VC investors and the companies in which they invest and (ii) the high standards of governance that are a feature of the PE/VC model, any mandatory reforms would not suitably address the concerns raised in the Green Paper. Mandatory reporting would increase the administrative burden placed on private businesses at a time when businesses are already implementing a number of reporting requirements covering the treatment of employees and suppliers.
- A better approach would be to focus on existing legislation and regulatory regimes that are designed to protect the stakeholders identified in the paper, such as employees, suppliers and pension fund beneficiaries.

- The Green Paper suggests the potential creation of a Corporate Governance Code for large private companies, based on the current UK Corporate Governance Code, which applies to quoted companies with a premium listing. Given the nature of the relationship between shareholders and listed companies is very different to that between a PE/VC-backed company and its shareholders, a code would not be suitable.
- Wider promotion of non-binding guidelines or principles covering best practice in reporting and corporate governance would be a more proportionate policy response to address concerns, rather than the introduction of a code aimed at private companies that requires further reporting (even if on a comply or explain basis). Any threshold or definition for large private companies intended to be captured by proposed reforms would also need to be based on carefully determined criteria (broader than solely employee numbers) in order to achieve any form of meaningful coverage.
- Private companies in the UK already adhere to high standards of reporting and transparency. The UK has enjoyed high levels of investment due to the stability of its legal system and quality of its reporting regime. Any additional reporting or administrative burdens, with the associated additional costs, would hamper the UK's competitiveness as a destination for investment and this must be borne in mind as the UK prepares to leave the EU.

Select Committee Conclusions

In its April 2017 report, the Select Committee acknowledged a number of the BVCA's assertions, noting that much of the evidence it had received agreed with the different treatment for corporate governance purposes of private companies relative to public companies, and argued that the imposition of greater regulatory burdens was not warranted. The Select Committee referred in particular to observations that, for most private companies, there is little separation between ownership and control, so the company would in effect be reporting to itself about itself on governance principles. The Select Committee also noted the argument that the sheer variety of private companies would make it difficult for a single governance code to be applicable to all.

Nevertheless, the Select Committee acknowledged the arguments in favour of greater transparency and accountability for private companies, based on the premise that those with a significant presence in the community (apparently assessed by reference to a company's size) have wider social responsibilities and should be required to report on non-financial matters for the benefit of employees and other stakeholders, as well as being subject to minimum standards of corporate social responsibility.

Importantly, the Select Committee agreed that it would not be sensible to simply apply the existing UK Corporate Governance Code to private companies and that an alternative is therefore required, with many models from which to choose including:

- the Institute of Directors' guidance for unlisted companies;
- the big four accountancy firms' voluntarily agreed FRC Code for audit firms;
- the code published by the European Confederation of Directors' Associations; and
- the Private Equity Reporting Group's monitoring and annual report on industry compliance with guidelines covering disclosure of information, which the Select Committee acknowledged to be an effective regulatory solution.

Whilst reiterating their desire for a new regime to build public trust by improving transparency and confidence in private companies by driving up standards of corporate governance and providing a mechanism for any potential failings to be flagged and pursued with the company concerned, the Select Committee expressed a preference for the development of a new voluntary code for large private companies with requirements (i) consistent with the existing comply or explain approach for listed companies and (ii) both proportionate and flexible, to reflect the diversity of companies potentially covered.

Specifically, the Select Committee advocated a light touch approach based on:

- large private companies (initially capturing those with 2000+ employees);
- providing specified information on websites, rather than in published annual reports, and on a comply or explain basis;
- potentially covering revenues, compliance with section 172 of the Companies Act 2006 (which imposes a duty on directors to promote the success of a company), company structure, executive pay, numbers of employees and pension scheme contributions.

Next Steps

In conclusion, the Select Committee recommended that:

- the FRC, the Institute of Directors and the Institute for Family Business, together with private equity and venture capital interests, develop an appropriate code with which the largest privately-held companies would be expected to comply and that these organisations contribute to the establishing of a new body to oversee and report on compliance with the code;
- the code includes a complaint mechanism, to allow the overseeing body to pursue complaints raised about compliance with the code, with the scheme being funded by a small levy on members; and
- if this voluntary regime fails to raise standards after three years, or reveals high rates of unacceptable non-compliance, then a mandatory regulatory regime should be introduced.

Consequently, the BVCA will continue to engage with relevant stakeholders and BEIS as they respond to the Select Committee's recommendations, and follow up on the responses to the Green Paper. The BVCA will continue to ensure that any proposals do not impose a disproportionate burden on privately held businesses.

05.

The New Private Fund Limited Partnership

Geoff Kittredge, Debevoise & Plimpton
Sally Gibson, Debevoise & Plimpton
Simon Witney, Debevoise & Plimpton

05. The New Private Fund Limited Partnership

On 6 April 2017, the UK government's long-awaited reforms to limited partnership law became effective. The BVCA made a number of recommendations to HM Treasury on how UK limited partnership law could be improved from the point of view of the private fund industry, and we are pleased to note that the government has taken on board many of the issues raised by the BVCA and incorporated them into the reforms. The effect of the changes is to create a new UK vehicle for private funds.

The Legislative Reform (Private Fund Limited Partnerships) Order 2017 (the "Reform Order") establishes a new fund vehicle known as a Private Fund Limited Partnership ("PFLP"). The Reform Order has come about as a consequence of the government's desire to increase the competitiveness of the UK asset management industry.

English or Scottish limited partnerships (referred to in this article as UK limited partnerships) have been a popular choice for private fund managers since 1987 when the government and the tax authority jointly confirmed certain aspects of their tax, legal and regulatory treatment. But, since then, the UK's competitive position over other European jurisdictions has been impacted by the reform of existing European vehicles, or by the introduction of new European vehicles.

The BVCA and other industry participants have long argued that some relatively small legal changes would enhance the attractiveness of the UK limited partnership and allow the jurisdiction to maintain its competitive advantage, particularly important in light of the UK's impending departure from the European Union. Despite many set¬backs to the pace of reform—including some last-minute fears that these changes would be further delayed—the BVCA welcomes the Reform Order as a timely modernisation of the UK Limited Partnerships Act 1907 (the "LP Act"), the primary legislation governing UK limited partnerships.

Geoff Kittredge
Debevoise & Plimpton

Sally Gibson
Debevoise & Plimpton

Simon Witney
Debevoise & Plimpton

Designation as a private fund limited partnership

New UK limited partnerships

On registration of a UK limited partnership on or after 6 April, the general partner may elect for that UK limited partnership to be designated as a PFLP, provided the UK limited partnership satisfies the following conditions:

- it is constituted by written agreement; and
- it qualifies as a "collective investment scheme" under the Financial Services and Markets Act 2000 (or would do so but for an exemption).

Existing UK limited partnerships

It is important to note that the new PFLP regime is voluntary and the changes will not apply to an existing UK limited partnership unless the general partner elects for that limited partnership to opt in to the PFLP regime.

For both new and existing UK limited partnerships, once a limited partnership is designated as a PFLP, it is not possible for the general partner of that limited partnership to take the limited partnership out of the PFLP regime.

Principal changes

The principal changes introduced by the PFLP regime relate to:

- the introduction of a "white list" of activities that limited partners may undertake without running the risk of losing their limited liability status;
- the easing of restrictions regarding capital; and
- the removal of other administrative burdens.

Importantly, the fundamental features of the existing limited partnership structure – which is familiar to investors and their advisers, and sits upon a body of well-understood law – are preserved. In particular, the changes have no impact on either the tax status of the limited partnership or the contractual freedom inherent in the vehicle.

"White list"

The Reform Order introduces a non-exhaustive "white list" of activities that a limited partner of a PFLP may perform without jeopardising its limited liability status. The concept of a "white list" or "safe harbours" is one that is an important component of the limited partnership legislation that governs limited partnerships established in "popular" fund formation jurisdictions such as the Cayman Islands, Delaware, the Channel Islands and Luxembourg.

If a limited partner of a UK limited partnership takes part in the management of the partnership business, it will have unlimited liability for the debts of that limited partnership incurred while it takes part in the management. However, there is no authoritative guidance on what taking part in the management of the partnership business means. As a result, there has been a degree of uncertainty as to what a limited partner of a UK limited partnership may do without jeopardising its limited liability status.

In general, the "white list" clarifies that limited partners may play some role in certain decisions of a PFLP without jeopardising their limited liability status. The list is drafted broadly and covers activities such as approving or vetoing investments, as well as more mundane limited partner involvement (e.g., approving accounts, appointing or nominating a person to represent the limited partner on the private fund's advisory committee and taking part in a decision in respect of a potential or actual conflict of interest).

The government took heed of the BVCA's recommendation that the list should be expressed as non-exhaustive, so as to avoid giving rise to an adverse presumption about activities that are not included on the "white list".

It is also important to note that the LP Act (now and post the Reform Order) does not prescribe rights that must be granted to limited partners. The rights of limited partners are dictated by the limited partnership agreement that governs the UK limited partnership.

Capital contributions

A limited partner in a PFLP is not required to contribute capital to that PFLP. Currently, a limited partner in a UK limited partnership must contribute capital on its admission as a limited partner in order to secure its limited liability status (i.e., capital must be drawn down from or advanced on behalf of a limited partner concurrently with its admission). There is no restriction on a limited partner of a PFLP withdrawing capital contributed to that PFLP during the life of that PFLP.

Currently, a limited partner of a UK limited partnership that withdraws capital contributed to that limited partnership during the life of that limited partnership will be liable for the debts of that limited partnership up to the amount of capital withdrawn.

The current "capital" rules in respect of UK limited partnerships have led to the development of a market practice whereby a limited partner makes a de minimis capital contribution on admission as a limited partner, with the remainder of its commitment advanced to the UK limited partnership as interest-free loans. This market practice will no longer be relevant for a UK limited partnership that is designated as a PFLP.

It is anticipated that the new capital requirements will simplify the accounting and closing process.

UK limited partnerships registered after 6 April 2017

For a UK limited partnership registered after 6 April but which is designated as a PFLP after registration, any capital contributions made by a limited partner to that UK limited partnership (whether made before or after designation as a PFLP) may be withdrawn free from any obligation imposed by the LP Act to return that capital contribution.

UK limited partnerships registered before 6 April 2017

For a UK limited partnership registered before 6 April but which is designated as a PFLP, any capital contributions made by a limited partner to that UK limited partnership prior to designation as a PFLP will remain subject to the current "capital" rules (i.e., if any such capital contributions are withdrawn, the limited partner will be liable for the debts of the UK limited partnership up to the amount of capital withdrawn).

Other administrative burdens

The Reform Order introduces a simplified registration process for PFLPs, with a reduction in the amount of information that has to be included in an application for registration (or following a change in the particulars) when compared with what is required for a traditional UK limited partnership. For example, the amount of a limited partner's capital contribution to a PFLP no longer needs to be notified to Companies House.

The Reform Order also abolishes the requirement under the LP Act to advertise publicly certain changes to a PFLP. The current requirement that an advertisement must be placed in the Gazette if, for example, a limited partner of a limited partnership assigns any portion of its interest in that limited partnership to another person will not apply to a PFLP.

There are also changes to make it easier for limited partners to arrange the winding up of a partnership. Current requirements for non-PFLPs prescribe that the general partner of a UK limited partnership must wind up a limited partnership, unless the limited partners obtain a court order to the contrary. Under the PFLP regime, the default position would still be that the general partner is responsible for the winding up of a PFLP, except where there is no general partner (e.g., following its removal at the election of the limited partners), in which case the default position would be that the limited partners would appoint a third party to wind up the PFLP. This power of appointment is expressly referenced in the "white list" and its exercise therefore will not jeopardise the limited partners' limited liability.

No change to legal personality

There was one notable reform recommended by the BVCA that was not incorporated into the Reform Order – the possibility of an English limited partnership being allowed to elect to have separate legal personality.

Scottish limited partnerships have separate legal personality, whereas those established elsewhere in the UK do not. The government has previously said that it will explore whether to introduce an elective regime, whereby on establishment the general partner of an English limited partnership could elect for that limited partnership to have separate legal personality. The introduction of an elective regime would require primary legislation and is therefore not included in the Reform Order.

Going forward

The BVCA has worked hard over many years to secure the changes introduced by the Reform Order. The creation of the PFLP regime is a welcome step and one that should help the United Kingdom to remain competitive as a jurisdiction for global fund formation in the face of competition from other jurisdictions.

06.

BEIS review of Limited Partnership Law

Ed Hall, Goodwin Proctor

06. BEIS review of Limited Partnership Law

Ed Hall
Goodwin Proctor

On 16 January 2017 (the same date as the final legislation for the greatly welcomed new Private Funds Limited Partnership regime was published (see p.29 for a full summary), the Department for Business, Energy and Industrial Strategy (BEIS) announced that they were separately launching a review of limited partnership law to ensure that the vehicle was not being used as an "enabler of crime".

This review followed a number of press stories, primarily in the Herald Scotland, about a "spike" in the numbers of newly formed Scottish Limited Partnerships ("SLPs"). This spike, coupled with some high profile cases linking SLPs to Eastern European organised crime and money laundering activities, has caused the Herald (and subsequently a number of members of parliament) to question whether SLPs are being widely used to facilitate crime.

While the press articles are focused around SLPs, BEIS has been clear that their review has wider scope and focuses on all UK limited partnerships ("UKLPs") – i.e. English limited partnerships and those established in Wales and Northern Ireland. Their review is considering the following areas:

- Understanding the Landscape
  - Why has there been a sharp increase in SLPs?
  - Are there reasons for this increase other than to enable criminal activities?
  - What are the most common legitimate uses of SLPs?

- Fixing the problem
  - How can the government reduce the potential for UKLPs to be used as enablers of crime without materially affecting their legitimate use?
    - Should there be greater transparency requirements on UKLPs?
    - Should there be greater requirements placed on formation agents that establish UKLPs for third parties?
    - Should there be greater restrictions on UKLPs that have no "nexus" to UK?
  - Should there be an ability to strike-off UKLPs from the public register (similar to the existing strike-off provisions in respect of UK companies), in particular where the UKLP is being used to enable criminal activity.

The BVCA provided a detailed response to BEIS' Call for Evidence and has been engaging with BEIS since then to emphasise the importance of UKLPs to the investment funds industry and assist BEIS in its review.

Understanding the Landscape

The "spike" in new SLPs

There can be little doubt that there has been a sharp increase in SLPs recently that is not easy to explain. BEIS' statistics show that while the number of non-Scottish UKLPs has increased steadily by about 5 per cent year on year for a number of decades, SLPs have increased by 30 per cent in the last year and by 239 per cent over the last five years.

While there are reasons to argue that SLPs have become easier to use in recent years (due to the easing of some of Scottish law formalities around execution of documents), it is hard to argue that the changes are sufficiently significant to justify the increase in registrations when compared to registrations of non-Scottish UKLPs. Therefore, short of BEIS finding a new legitimate rationale for the recent increase in the number of SLPs, suspicions will continue that they are being used for illegitimate reasons.

Legitimate use of SLPs

The BVCA has, of course, emphasised that while UKLPs may be being used for illegitimate purposes (as may a wide range of other UK and non-UK vehicles), their use for legitimate reasons and in particular as a part of the investment funds landscape is of fundamental importance.

In our view, the popularity of UK limited partnerships is an important reason for the dominance of the UK as a centre for private equity and venture capital. Private equity and venture capital firms are long-term investors, typically investing in unquoted companies for around three to seven years. Private equity and venture capital managers generally exercise a great level of influence over the businesses they own, and undertake important strategic and operating initiatives to create value and enhance the performance of businesses owned. There is a commitment to build lasting and sustainable value in business and as a result strong returns for investors in private equity and venture capital funds as described below. BVCA members have invested over £27bn in nearly 3,900 UK-based companies over the last five years. Private equity and venture capital funds managed in the UK currently back around 2,980 companies, employing over 900,000 people on a full-time equivalent basis (“FTEs”) across the world. Of these, around 385,000 FTEs are employed in the UK and 333,000 are employed in the rest of the EU. In 2015, 34 companies experiencing trading difficulties were rescued by BVCA member firms, helping safeguard around 16,500 jobs.

The continued attractiveness of UKLPs is especially important in the context of Brexit where current uncertainty may tempt a number of fund managers towards continental European structures in Luxembourg, Ireland or the Netherlands or towards offshore centres like Jersey or Guernsey. Given the extremely welcome introduction of the Private Funds Limited Partnership regime, it is critical that the UK does not place new restrictions on these structures that diminish their new benefits.

Fixing the Problem

Transparency

While UKLPs may be being used to facilitate crime, it seems unlikely that this is due to the lack of existing transparency obligations. In fact UKLPs are considerably more transparent than their direct competitors. In particular, the obligation to make public (and keep updated) a full list of both general partners and limited partners is not a requirement in other commonly used limited partnership structures, whether in EU jurisdictions such as France and Luxembourg, offshore jurisdictions such as Jersey and Guernsey or in “rest-of-world” limited partnerships such as those used in the USA and Canada.

Also, as a result of the Fourth Money Laundering Directive, SLPs (although not other UKLPs) will need to create a and maintain a public Persons of Significant Control (“PSC”) register in the same way as UK companies and LLPs from July 2017, creating additional transparency requirement for those partnerships.

Establishment and Formation Agents

If it isn’t due to lax transparency requirements, it may simply be the case that SLPs are being used due to the ease of establishment, and BEIS may focus on this aspect in any proposed reforms. There appears to be a particular focus in BEIS’ review on the role of formation agents in the establishment of SLPs.

BEIS have identified the fact that twelve UK-based formation agents established 75 per cent of the 2,878 SLPs that were registered in the period from December 2015 to June 2016. In some cases, several hundred SLPs were established by the same formation agent in a single day. Most of these formation agents are already regulated; either as lawyers/ accountants or as “Trust or Company Service Providers” and are required to comply with existing Anti-Money Laundering requirements that are designed to identify suspicious activity. It may be that there is a greater focus on supervision and enforcement of these rules against existing formation agents.

There is clearly some benefit in using existing enforcement powers in preference to creating additional restrictions or administrative hurdles. In particular if there are just one or two “rogue” formation agents that are establishing partnerships without fulfilling their anti-money laundering obligations then intervening at this level may result in the problem being stopped as quickly as it started, without affecting legitimate businesses.

A UK Nexus?

Another area of BEIS’ focus is on UKLPs that have no obvious nexus to the UK. This is an area of considerable sensitivity to the investment funds industry as one of the key structuring benefits of UKLPs is the ability to admit non-UK partners and to manage the partnership from a principal place of business that need not be within the UK. Investment funds typically have a life of 10-15 years and it is very difficult and expensive to change the fund vehicle during the fund life. However, in a UKLP it is possible to change the place of management of the fund without changing the fund vehicle itself. This is particularly important in the context of Brexit where investments funds need to be able to demonstrate to their investors that they are able to react to an, as yet unknown, post-Brexit legal and regulatory landscape.

There is also a question in the Call for Evidence about the potential impact of requiring a “presence in UK” for UKLPs at all times (i.e. the equivalent to a company’s Registered Office). However, the interaction between this and the EU Alternative Investment Fund Managers Directive (AIFMD) could result in a materially adverse impact on a large number of investment funds that have a principal place of business outside of the EEA. Broadly, the test for whether an investment fund is subject to the AIFMD (an “EU AIF”) is whether its registered office is within the EEA. The FCA take the view, because there is no registered office concept for UKLPs, that the question of whether a UKLP is an EU AIF or not depends on whether its “principal place of business” is within the EEA. Therefore, the introduction of a registered office requirement could have the effect of immediately converting a large number of non-EU AIFs into EU AIFs. Under the AIFMD an EU AIF cannot currently be managed by a fund manager outside the EEA and so a large number of fund managers would be immediately in breach of the AIFMD and/or would have to establish a fund management entity in, say, Luxembourg at considerable expense to both the manager and the fund’s investors.

Strike-off powers

Finally BEIS is considering the benefits of creating a “strike-off” regime for UKLPs. Currently there is no ability for either the general partner or the UK Registrar of Companies to remove UKLPs from the public register of limited partners. This means that the limited partnership register includes limited partnerships that were fully liquidated many years ago. Therefore, there would likely be general support within the industry for a mechanism to “clean up” the register of limited partnerships.

However, there is a legitimate concern about what that would mean in practice. In particular, from a legal perspective, a general partnership is simply the relationship of “persons carrying on a business in common with a view to profit” and a limited partnership is just a general partnership that has registered for limited partnership status, thereby providing limited liability protection to certain of its partners. Consequently while a company that is struck-off the register simply ceases to exist, a limited partnership that is struck-off the register could be viewed as defaulting to general partnership status, on the face of it resulting in the limited partners losing their limited liability protections.

This limited liability protection is a fundamental requirement for investment funds; put simply an investor will not invest in a structure where there is a risk of it having unlimited liability. Losing limited liability does not just mean that the investor is liable for their share of the partnership's liabilities (which they would have if they had invested directly in the relevant assets), but could result in the investor being liable, on an uncapped basis, for every other investor's share of the partnership's liabilities.

Therefore if there is to be some mechanism for strike-off of partnerships, (and in particular if it can be enacted by the registrar), it is vitally important that it is clear that this does not result in limited partners losing their limited liability protection.

Next Steps

The Call for Evidence concluded on 17 March 2017 and BEIS are now reviewing the responses that they have received. Based on those responses they will consider what next steps should be taken. While the timeline for that is not clear, it is hoped that any recommendations taken are sensible and proportionate; enabling the government to tackle crime without creating material burdens or restrictions on legitimate enterprises.

07.

Case Law update

Ed Griffiths, DLA Piper

07. Case Law update

Applying the principle of informal unanimous consent (the Duomatic principle)

Ed Griffiths
DLA Piper

In its decision in *Randhawa & Ors v Turpin & Anor*, the High Court considered whether the appointment of administrators by the company's sole director was invalid as the company's articles of association limited the powers of a sole director to convening a general meeting or appointing an additional director and any other decisions required a board meeting quorum of two. The sole director held 75 per cent of the company's share capital on bare trust for his father, with the other 25 per cent registered in the name of a company which had been dissolved (with the father being the probable beneficial owner).

The court held that the administrators' appointment was valid. It found that there had been a consistent course of conduct under which the company's shareholders and beneficial owners had informally sanctioned the exercise of all the directors' powers by one director alone which thereby operated as an informal amendment to or variation of the articles, and which was binding on the company under the principle of informal unanimous consent (ie the *Duomatic* principle). The principle provides that, if all the shareholders of a company who can vote at general meetings agree to a matter that could be approved at a general meeting, that matter is binding as if a resolution had been passed in general meeting to that effect. In the circumstances, the court considered that the acquiescence of the 75 per cent shareholder alone ought to be sufficient to trigger the Duomatic principle, as no one could have voted the remaining 25 per cent (the registered holder no longer existed and no-one else was on the register of members in its place).

Meaning of "close of business" and "commercial banks"

The case of *Lehman Brothers International (Europe) (In administration) v ExxonMobil Financial Services BV [2016] EWHC 2699 (Comm)* considered the phrases "*close of business*" and "*commercial banks*".

Here, a notice was deemed received on a particular day if it was received before "close of business", which was not defined further. ExxonMobil had submitted a notice to Lehman's London offices at 6.02 pm. Lehman argued that a reasonable person would regard "*close of business*" in London as 5 pm. ExxonMobil argued that this should be 7 pm. The judge considered that in the context of financial business of the kind at issue, a reasonable person might be surprised to hear that business closes at 5 pm. The judge also said that the contract could easily have imposed an express cut-off time, but it did not do so. The onus was on Lehman to establish when close of business occurred (as the party alleging that the notice arrived too late). As Lehman had failed to put forward any admissible evidence, that was sufficient to decide the point in favour of Exxon.

The court also considered close of business for "*commercial banks*" in London, which was used in a proviso to the notice clause. Lehman argued this expression pointed towards what might be called normal business hours, such as are worked by ordinary businesses and High Street banks, rather than the later hours worked by investment bankers, commercial lawyers and the like, which supported their contention of 5 pm (or even earlier). The judge did not accept this. Although there was a working definition from the Financial Times Lexicon put before the court, his view was that the expression "commercial banks" did not have any particular meaning in English law. Lehman's experts did not give evidence on the point. The only evidence came from Exxon's expert, who said that though this is a necessarily rough approximation, in the modern world commercial banks closed at about 7 pm. The judge said that he saw no reason not to accept his evidence, but made it clear that this was a finding of fact limited to the present case.

From a drafting perspective, “close of business” terminology offers a certain amount of flexibility. However, if left undefined, this could be interpreted by reference to other contexts which may not be the parties’ intention. To ensure certainty, it may therefore be preferable to define “close of business” by reference to a specific time (addressing different time zones, if relevant).

Effectiveness of investment presentation disclaimers

In *Taberna Europe CDO II plc v Selskabet*, the Court of Appeal confirmed that non-reliance statements and statements denying liability for errors and omissions, commonly included in disclaimers in investment presentations and information memoranda, are in principle effective to exclude or limit liability for misrepresentation. In reviewing such statements, the court will recognise that commercial parties are entitled to make their own bargain and interpret fairly the language used (which was held to be clear in this case). The decision reversed an earlier High Court decision which held that such disclaimer language was ineffective. The Court of Appeal made it clear in this decision that, in order for a representation in a document to be actionable, there needed to be a connection between the issuer and end investor so that it is clear that the issuer was intending the investor to rely on the document. Simply having material accessible on the internet is insufficient, but where an investor is specifically directed to the material, the issuer cannot complain if the investor seeks to rely on it, subject to any disclaimers within the material. The court also took the view that a document such as an investor presentation should be able to specify that information in it is provided on the basis that the issuer is not taking responsibility for it, provided that this is reasonable.

This case therefore highlights the importance of setting out the basis on which information is shared before entering into a transaction. It should be noted that the parties were both sophisticated and therefore extra care will need to be taken if dealing with less sophisticated parties.

Interpretation of an indemnity in a share purchase agreement

In *Wood v Capita Insurance Services Limited*, the Supreme Court considered the true construction of an indemnity in a share purchase agreement of an insurance broker. The seller was to indemnify the purchaser in respect of:

“*all actions, proceedings, losses, claims, damages, costs, charges, expenses and liabilities suffered or incurred, and all fines, compensation or remedial action or payments imposed on or required to be made by the company following and arising out of claims or complaints registered with the FSA…pertaining to any mis-selling or suspected mis-selling…*”

in the period before the sale. Following completion, the company referred itself to the FSA as it found that mis-selling had occurred prior to the sale. The FSA directed the company to pay compensation to its affected customers, which the purchaser sought to recover under the indemnity.

The seller argued that the indemnity didn’t apply as the purchaser’s losses arose from the company’s referral of itself to the FSA, rather than as a result of a customer claim or complaint. The purchaser, however, argued that the indemnity did apply as the words “*following and arising out of claims or complaints registered with the FSA*” only applied to “*all fines, compensation or remedial action or payments imposed on or required to be made by the company*” limb.

The Supreme Court agreed with the Court of Appeal's decision that the indemnity was limited to loss that followed or arose from a customer claim or a complaint registered with the FSA. On the approach to contract interpretation, the court observed that *Arnold v Britton and Rainy Sky SA v Kookmin Bank* were saying the same thing, and re-emphasised that contract interpretation is a unitary exercise that requires striking a balance between the indications given by the language used, having regard to the contract as a whole, and the practical implications of competing constructions. Textualism and contextualism can both be used as tools to ascertain the objective meaning of the language used in a contract, but the extent to which each tool will assist will vary according to the circumstances. Where there are rival meanings, the court can reach a view as to which construction is more consistent with business common sense, but in striking the right balance, the court must consider the quality of the drafting, and be alive to the possibility that one side has struck a bad bargain.

Scope of legal professional privilege

In *Re The RBS Rights Issue Litigation*, the High Court ruled that records of interviews with employees and former employees of RBS carried out by the bank's lawyers during an internal investigation were not privileged. The judge held that legal professional privilege is strictly confined to communications between a lawyer and his client for the purpose of giving or receiving legal advice. The concept of "client" for the purposes of privilege is to be narrowly interpreted and consists only of those employees of the company who were capable in law of seeking and receiving legal advice as a duly authorised organ of the corporation. The interviewees had been authorised to provide information to the lawyer, but this did not make them a client.

The judge also rejected the bank's alternative claim that the records of the interviews made by the lawyers were privileged on the basis that they were "lawyers' working papers". Lawyers' working papers can be considered privileged under English law if their disclosure would reveal or give a clue as to the trend of advice given to a client by its lawyer. The Court found that there was insufficient evidence that the documents would betray, or at least give a clue as to, the trend of legal advice provided to RBS.

This decision highlights that where legal professional privilege does not apply because no litigation is contemplated at the time of an employee interview, lawyers should not operate under the assumption that their notes of the interview are privileged. Telling the interviewees that the interview notes will be confidential and subject to "attorney-client privilege" will not necessarily mean that this is the case.

Costs awarded under a contract which refers to "reasonable attorney fees" on standard or indemnity basis?

In *Euro-Asian Oil SA v Credit Suisse AG*, the court held that costs that were being awarded to a successful claimant in accordance with contractual provisions which expressly provided that the costs should be limited to "*reasonable attorney fees*" should be confined to costs on a standard basis. The claimant had argued that it should be awarded costs on an indemnity basis. The court held that indemnity costs cannot be regarded as reasonable and so the claimant was only entitled to costs on a standard basis and not on an indemnity basis.

The practical point to be taken from this case is that if you include the word "reasonable" in this kind of context in relation to costs, you may rule out the possibility that the court will award indemnity costs.

Scope of cross-border mergers

In *Re Easynet Global Services Limited*, the High Court held that the proposed transaction, to merge a number of UK companies and a Dutch company into a UK transferee company, was not the kind of transaction which the Companies (Cross-Border Mergers) Regulations 2007 (which implemented the EU Cross-Border Mergers Directive in the UK) was enacted to facilitate. It found that the Dutch company (which was dormant, had never traded and had no appreciable assets) had only been included as a “device” to bring the transaction within the scope of the Regulations. The court considered that a purposive approach should be taken to the interpretation of the Regulations and while the transaction could be said to be a merger, it was not, in reality, a cross-border merger. If the court’s interpretation was wrong, then it held the fact that it was within the Regulations due to this “device” was something that the court could and should take into account at the discretion stage, when it considers whether to sanction the merger.

The case highlights that there needs to be a genuine cross-border element to come within the scope of the Cross-Border Merger Regulations. Domestic mergers will need to use an alternative structure.

First “reverse” cross-border merger

In *Re Formenta Limited*, the High Court sanctioned the first “reverse cross-border merger by absorption”, approving a UK holding company being merged into its Italian subsidiary (thereby changing the group from a UK one to an Italian one).

The Companies (Cross-Border Merger) Regulations 2007 do not recognise the concept of a reverse cross-border merger, but Italian law and the EU Cross-Border Mergers Directive (which the Regulations implemented) do. The court dealt with the issue by treating the merger in the same way as a merger by absorption of a wholly owned subsidiary, but rather than the transferor being the subsidiary that is merged into the parent company, the transferor was the parent company that was merged into the subsidiary. The underlying argument for why the cross-border merger procedure should be available for both reverse and forward cross-border mergers was that where the merger takes place between wholly owned entities, it is effectively a matter of internal reorganisation, with no material impact on shareholders. Accordingly, the court indicated that it saw no problem with the concept of a reverse cross-border merger and approved the application.

With Brexit on the horizon, we may see this “reverse” cross-border merger used as way of re-domiciling companies from the UK to Europe.

Cancellation scheme of arrangement in connection with a takeover

In *Re Home Retail Group Plc*, the High Court had to determine whether a cancellation scheme following the sale of a business, to be carried out in connection with a takeover, fell within the anti-avoidance provisions in sections 641(2A) and 641(2B) of the Companies Act 2006. These provisions prohibit a company from reducing its share capital as part of a scheme of arrangement where the purpose of the scheme is to acquire all the shares of the company, except where the acquisition amounts to a restructuring that inserts a new holding company into the group structure. They were introduced to block a common stamp duty savings scheme previously used on takeovers.

In this case, the company had announced that it had agreed to sell its DIY retail business and that it would make a capital return to its shareholders of the net cash proceeds of the sale. Before the sale had been completed, the company reached agreement in principle on a takeover by another company. The consideration that the bidder was to pay took into account that the company would be returning capital to shareholders. The overall plan was to be effected in stages:

- first, a scheme of arrangement under which a new company would become the company's holding company, with the company's existing shareholders essentially obtaining corresponding holdings in newco;
- second, a reduction of capital of newco to effect the previously announced return to shareholders; and
- finally, the shares in newco would be compulsorily transferred to the bidder in accordance with newco's articles of association.

The court held that there was no doubt that the holding company exception in section 641(2B) applied to the scheme if it was read literally, but the parties sought confirmation that they would not be denied use of the exemption based on the application of the *Ramsay* principle of purposive construction. The principle, from the case of *W T Ramsey Ltd v Inland Revenue*, provides that *"the ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically"*. The court declined to decide whether the *Ramsay* principle applied to section 641(2B). However, the court decided that even if the principle was capable of applying, it would not bite on a cancellation scheme which was part of a real world transaction having a clear commercial and business purpose. The cancellation scheme envisaged here was of that type and therefore had the benefit of the exception.

The decision therefore provides some comfort that the courts will take a pragmatic approach and a cancellation scheme of arrangement forming part of a wider plan involving a takeover will not be prohibited under section 641(2A) as long as it has a genuine commercial purpose.

Takeovers by way of scheme of arrangement: first court decision on share-splitting

A scheme of arrangement has to be approved by members who represent 75 per cent in value and by a majority in number of members. A tactic of members opposed to a takeover has been to split their shareholding into smaller holdings with the aim of increasing the number of members voting against the scheme of arrangement, so that even if 75 per cent of members in value approve the scheme such members do not represent a majority in number of members resulting in the scheme of arrangement failing.

In *Re Dee Valley Group plc*, this share-splitting tactic was adopted. Here, one individual gifted shares to 443 separate individuals with the aim of defeating the scheme of arrangement. The chairman of the court meeting excluded the votes of the 443 individual shareholders who derived their shareholding from the individual who opposed the scheme. Consequently, the statutory requirements to approve the scheme of arrangement were met and the High Court sanctioned the scheme of arrangement.

The High Court held that members voting at a class meeting directed by the court must exercise their power to vote for the purpose of benefiting the class as a whole, and not merely individual members only. The court concluded that the chairman of the court meeting was right to reject the votes of the individual shareholders who derived their shareholding from the share-splitting exercise. The court stated that the chairman was justified in concluding that the only possible explanation for the conduct of those shareholders in each accepting a gift of a single share immediately after the court meeting had been directed was to further a share manipulation strategy to defeat the scheme. The court was entitled to protect the integrity of the court meeting against manipulative practices such as share splitting that would frustrate its statutory purpose.

Effect of filing incorrect articles at Companies House

In *Gunewardena v Conran Holdings Limited*, the High Court considered whether failure to file a correct copy of the articles at Companies House affected their validity. The company's 1993 articles contained compulsory transfer provisions upon employee shareholders leaving the company. In 1995 the valuation mechanism in the articles was amended. The articles were amended again in 1998, on the creation of a new class of shares, but they still included the revised valuation mechanism introduced in 1995. In error, the company's solicitor filed the 1993 version of the articles at Companies House, rather than the 1998 version.

The court held that the 1993 version of the articles of association that had been erroneously filed at Companies House was not the actual articles of association of the company. The current and valid articles of association of the company were clearly those that had been most recently resolved upon by the members (ie the 1998 version of the articles which included the 1995 valuation mechanism). If the members resolved on an amendment by special resolution, the amended articles became the new contract and the new articles, and took effect immediately. Their status as the articles of the company did not depend on registration and an erroneous filing did not affect the form of the articles as had been validly resolved upon by the members.

Share buybacks and the obligation to "pay" on completion

In *Dickinson v NAL Realisations (Staffordshire) Ltd*, the High Court had to determine whether a buyback of shares contravened the Companies Act 2006. Here, the company agreed to buy back most of the issued shares at par for a total consideration of £2.5mn. Much or all of the consideration was left outstanding on director's loan account, and subsequently secured by the company executing a debenture. The court held that the arrangements for the purchase price to be left outstanding on loan account at completion did not amount to "payment" on purchase as required by section 691(2) of the Companies Act 2006. The judge rejected that the loan arrangements were in the circumstances to be treated as payment and held that where the consideration payable was not actually satisfied at the time, a debt automatically arose. Acknowledgement of that debt by entering into a loan agreement did not constitute payment on purchase and it would be wholly artificial to regard such an agreement as creating an obligation to pay money to a company by way of loan which was then set off against the company's obligation to pay the purchase price. The buyback was therefore held to be void.

The judge in the case did however comment that very similar results could be achieved by structuring the transaction so that money was actually paid by the company at completion and an equivalent amount was very shortly thereafter paid back to the company by way of loan. Alternatively, it might borrow in advance from a third party and use the funds to pay the selling shareholders. Provided in each case that the two transactions were genuinely separate, such that the arrangement was not a sham, the judge commented that they should satisfy the requirements of section 691(2).

08.

EMIR update

Louise Dumican, Carlyle

08. EMIR update

Louise Dumican
Carlyle

Entities in the European Union which have entered into derivatives contracts (including hedging agreements such as swaps, options and forwards) are subject to obligations under an EU regulation referred to as "EMIR" or the "European Market Infrastructure Regulation" (No 648/2012). While principally directed at firms which actively trade derivatives such as hedge funds, EMIR has had a material impact on funds which invest in private markets but use derivatives to hedge currency and interest rate exposure.

Any entity in Europe which has derivatives outstanding has obligations under EMIR which require action to be taken. Regulated entities (including AIFs managed by authorised and registered AIFMs but excluding AIFs not managed by registered AIFMs) are subject to more onerous requirements.

The requirements of EMIR are being implemented in stages from 2012 with the full requirements to be in effect by 2020. The requirements can be broken down into two groups:

- administrative requirements such as record keeping, confirmation of transactions, reconciliation of trade data, reporting of transactions to a central database referred to as a trade repository and the putting in place of dispute resolution procedures which can generally be dealt with relatively easily; and
- central clearing requirements and collateral/ margining requirements for derivative contracts that are not centrally cleared, which are operationally burdensome and have material costs associated with them.

The provision of collateral or margin consists of the provision of money or securities as collateral to a counterparty in an amount designed to reduce the credit risk which the recipient is exposed to with respect to the party posting the collateral i.e. the more risk a collateral receiver is taking the more collateral it will expect. Requirements to post collateral make it more expensive to enter into derivatives contracts and may reduce the attractiveness of hedging.

Central clearing involves interposing a company known as a clearing house between two parties to a derivatives contract which effectively becomes counterparty to both of them under two new, separate transactions. The clearing house takes collateral from both parties and is supposed to operate such that the default of a party to a derivatives transaction causes no loss to other market participants (due to the amount of collateral it holds). Effectively the clearing house is the counterparty for all centrally cleared derivatives transactions.

Which of the obligations of EMIR apply to an entity depend on which category it falls into. In simplified terms, unregulated entities within a fund structure such as portfolio companies should not be subject to central clearing and margining requirements whereas funds regulated under the AIFMD will be. All EU entities however, are subject to the administrative obligations.

In practical terms, fund groups which do not use regulated entities for hedging have simply had to tolerate the increased administrative burden imposed by EMIR. However, margining requirements have applied to most regulated entities from 1 March 2017 in respect of most types of derivative contracts and will come into effect in relation to physically-settled FX swaps and forwards during 2018. This is clearly an issue for fund entities which do not have easy access to liquid cash.

The European Commission has recently proposed some changes to EMIR which would increase the category of funds which are subject to the more onerous provisions of EMIR such as central clearing and margin posting to include AIFs not managed by registered AIFMs.

09.

Update on MiFID II: key issues for private equity and venture capital firms

Tim Lewis, Travers Smith

09. Update on MiFID II: key issues for private equity and venture capital firms

Tim Lewis
Travers Smith

Despite the result of the UK's referendum on membership of the European Union, there is unlikely to be a delay to the implementation of the recast Markets in Financial Instruments Directive ("MiFID II") and Markets in Financial Instruments Regulation ("MiFIR") which is due on 3 January 2018. The FCA has published the first set of its finalised rules at the end of March 2017. It is expected to publish the remaining rules by 3 July 2017.

Scope

MiFID II will affect all UK private equity and venture capital firms. The impact will differ depending on the manner in which firms are structured. The greatest impact of MiFID II will be on firms structured as MiFID managers whose activities are the main focus of recast legislation. There will also be a direct impact on firms structured as MiFID adviser/arrangers, although the application of MiFID II is more limited due to the more limited range of activities carried on by this type of firm.

The FCA is also proposing to "gold-plate" MiFID II by applying parts of it to full scope AIFMs, small AIFMs and residual CIS operators. This means UK based private equity and venture capital managers will be impacted by the changes even if they are not MiFID firms. In particular, the FCA is proposing to extend the research and inducements, best execution and telephone taping rules and confidentiality and data security requirements to these non-MiFID managers.

Key issues

Firms will be impacted by many of the changes arising out of MiFID II. We identify below some of the key issues:

Research and inducements: The biggest change to the current MiFID I inducements regime introduced by MiFID II is the ban on firms which provide portfolio management and independent investment advice from accepting and retaining fees, commissions or any monetary or non-monetary benefits from third parties (or persons acting on their behalf). There is a prescribed list of benefits which are excepted from the ban. These must be disclosed to clients. As regards the payment of inducements by portfolio managers and investment advisers, the existing MiFID I inducement rules will broadly be carried forward, except that such firms will need to comply with stricter rules to evidence that any payment made in connection with investment services is capable of enhancing the quality of the service provided. Firms will need to identify what constitutes an "inducement" and identify whether any changes are needed to their current arrangements for paying or receiving inducements in order to comply with the new regime.

Recording telephone conversations, electronic communications and other communications: Under the FCA's proposals, firms would be under an obligation to record any telephone conversations or electronic communications that are intended to result in the performance of regulated activities, whether or not they actually involve the performance of those activities. The FCA also proposes to implement rules requiring certain face-to-face conversations to be recorded. These are very widely drafted obligations. The BVCA and others have asked the FCA to narrow the scope of the regime to cover only those conversations in which an investment decision is taken. Firms will need to identify which types of conversation fall within the final ambit of the rules and may need to change their systems and controls (including potentially investing in new IT systems) to ensure they can comply.

Client categorisation: Local authorities will be classified as retail clients under MiFID II by default. This will affect firms dealing with UK Local Government Pension Scheme investors. Firms running funds which only accept professional clients will in future need to "opt-up" local authorities to professional client status. The FCA has proposed new tests for "opting up" UK local authorities to elective professional client status, but has noted that UK firms dealing with local authorities of another EU Member State should use the tests prescribed by that jurisdiction. Firms will need to adjust their processes when dealing with LGPS administrators as a result of the change.

Best execution: MiFID II makes a number of changes to the best execution regime for MiFID managers and advisor/arrangers which will require them to update their existing policies and disclosures. It also requires firms that execute or transmit client orders, or carry out the activity of portfolio management, to publish an annual report setting out certain information on the top five execution venues in terms of trading volumes used by the firm in the preceding year. In relation to transactions in unlisted securities, firms may be able to argue that there is no "execution venue" for the purposes of the new disclosure requirement.

Data security: MiFID II requires firms to maintain sound data security mechanisms to maintain the confidentiality of data, guarantee the security and authentication of the means of transfer of information, minimise the risk of data corruption and unauthorised access and prevent information leakage. Firms should generally have such systems in place but a review may be beneficial, particularly given that firms will need to undertake a review of their data protection arrangements prior to the implementation of the General Data Protection Regulation which will take effect on 25 May 2018.

Next steps

Firms should review the policy papers published by the FCA setting out the final UK rules implementing MiFID II. In the months leading up to the implementation date, firms will need to update policies and procedures, contractual arrangements and some will need to undertake substantial IT builds.

10.

The Fourth Money Laundering Directive

Paul Ellison, Macfarlanes

10. The Fourth Money Laundering Directive

Paul Ellison
Macfarlanes

The Fourth Money Laundering Directive ("4MLD") is designed to encourage a more risk-based approach to anti-money laundering ("AML") requirements whilst tightening perceived areas of weakness under the predecessor anti-money laundering regime. As such, 4MLD represents the EU's response to the latest AML and counter-terrorist financing ("CTF") standards, agreed by the Financial Task Force ("FATF"), the international AML and CTF body set up by the G8, and is designed to strengthen the EU's defences against money laundering and terrorist financing.

EU Member States are required to transpose 4MLD by 26 June 2017 but HM Treasury only published its consultation on the new Money Laundering Regulations 2017 (the Regulations) on 15 March this year. This gives firms only a very short window in which to update their AML policies and procedures to comply with 4MLD.

A flexible approach to money laundering risks

Despite 4MLD gathering further forces in the fight against crime and terrorism, certain key principals of flexibility and proportionality, which are positive for private equity managers, remain hard-coded into the legislation, both at 4MLD level and in the new draft Regulations.

For example:

- 4MLD promises a tailored and proportionate approach for the business of the so-called "obliged entities" which fall within its scope. Private equity managers should take comfort that the specific needs and nature of the private equity industry do not have to be ignored. The new regime also builds upon, rather than casting aside, the key themes of its predecessor legislation; and
- a holistic risk-based approach to money laundering requirements is still considered appropriate, using evidence-based decision-making. Box-ticking AML/CFT requirements in a way which leads to delays and inefficiency in business is not the intention.

However, as so often in the context of financial services legislation, the devil for private equity managers is likely to lie in some of the detailed provisions of 4MLD which, taken together, may represent an increase in the practical compliance burden imposed on private equity managers. We outline each of these key changes below.

Due diligence on underlying beneficial owners

A good example of the need to consider the detail, is the new definition of "beneficial owner" which is used in the core provisions on customer due diligence measures. At first glance, not much is changing in the definition set down in the Regulations. However, in the context of a trust it appears that any beneficiary under that trust will be deemed to be a "beneficial owner" subject to due diligence measures, even if they hold only a tiny minority stake.

This apparently small change removes the 25 per cent de minimis threshold which applies under the current 2007 Money Laundering Regulations, and risks vastly expanding the scope of the customer due diligence exercise which will need to be done, particularly in the UK where trust structures are much more prevalent than other EU jurisdictions. A de minimis beneficiary under a trust may be difficult to contact or verify from a due diligence point of view, leaving the onus and regulatory risk on the private equity manager to decide if it has taken "reasonable measures" under the legislation or must walk away from a potential deal, even though the de minimis beneficiary will have no real control over the trust.

Unfortunately it seems highly unlikely HM Treasury will adjust these provisions in the final draft of the Regulations following consultation, because the wording mirrors the provisions of 4MLD. Nevertheless, it is to be hoped that holistic and risk-based decision making will temper these new provisions to some extent, although firms will be required to adhere the warning in 4MLD that adopting a risk-based approach should not be interpreted as an "unduly persuasive option". It is likely that industry practice will evolve following the implementation of 4MLD to establish new norms, as firms determine how best to apply a risk-based approach. In doing so, firms are likely to find the guidance published by the Joint Money Laundering Steering Group (the "JMLSG") of value in calibrating their approach.

Correspondent banking

Also of potential impact upon private equity managers are the new provisions on correspondent banking (where a bank provides financing through a third party bank, often overseas). In the Third Money Laundering Directive ("3MLD") the concept of a "correspondent relationship" was not defined but this has been highlighted as an area of key risk by FATF because a so-called correspondent bank has no direct relationship with the underlying parties to a transaction and is not in a position to verify identities. They may also have limited information regarding the nature and purpose of underlying transactions.

Where a correspondent relationship exists, banks will need to carry out more onerous, enhanced due diligence ("EDD") on the customer. However, the definition of "correspondent relationship" is extremely broad and seems likely to capture legitimate private equity transactions which are in reality low risk. Although HM Treasury has promised that a measure of flexibility is required in the implementation of these requirements to avoid unnecessary drag on the real economy, the risk is that cautious and prudent banks will feel they have little room for manoeuvre in practice. These new requirements may therefore present issues and/or delay in otherwise completely legitimate cross-jurisdictional private equity deals.

Reliance on third parties

One measure designed to streamline the customer due diligence process and to prevent repetition is the right to rely on third parties' due diligence measures. In the PE industry, where transactions can be complex and involve multiple stakeholders there may be some reliance by managers upon banks and other firms conducting searches on wider business relationships, outside the immediate regulatory relationship between the PE manager and its client.

The 4MLD supports these measures emphasising the risks of delays and inefficiency in business where there are repeated customer identification procedures. In its consultation response, the government also expresses the wish to tackle the current barriers to firms using reliance.

However the drafting of the legal provisions in the Regulations is somewhat unsatisfactory and leads to the rather illogical regulatory outcome that reliance by a PE manager on another firm which is also directly subject to the Regulations involves more procedural steps and requirements than an outsourcing to a completely unregulated third party in a high risk country, even though the ultimate responsibility and liability of the PE manager is exactly the same in both cases.

Overall it is certainly questionable whether these new provisions are sufficiently attractive to convince firms to change current practices and rely more on third parties. In reality, the majority of firms carry out their own CDD because the risks and hassle of relying on third parties are seen as too burdensome. Where firms are still responsible for "any" failure to carry out CDD, it is likely that the safer option will be to continue to conduct all CDD measures.

A firm which is subject to the Regulations also has good reasons to refuse to allow other firms to rely upon it. Besides the obligation to enter into a written agreement to provide CDD information, the firm which conducts CDD must be in a position to provide full due diligence documentation to the relying party within two working days of a request. It seems inevitable that firms will struggle to commit to these stringent timeframes.

PEPs

A more controversial and widely debated aspect of the changes is the new provisions for politically exposed persons ("PEPs"). Although 4MLD emphasises that requirements in relation to PEPS are of a preventative rather than criminal nature and should not be used to stigmatise PEPs, nevertheless both 4MLD and the new Regulations extend the EDD requirements, which currently apply to foreign PEPs, to domestic PEPs, and to the family members and close associates of PEPs.

However, the UK has taken a relatively pragmatic approach in implementing this area of 4MLD, recognising that not all PEPs or associates of PEPs present a high risk and that the CDD measures imposed should be proportionate and not unduly burdensome.

In reality, given the risk-based approach, these provisions ought to pose minimal issues to private equity managers or represent a great change to current practice. However, as with the other areas where discretion is afforded to firms under the risk-based approach, the key challenge will be in deciding when to apply less stringent CDD. This may increase the burden on cautious firms and there is a danger that large institutions such as banks will decide it is safer to err on the side of caution and adopt a blanket policy for all PEPs.

The expectation is that the FCA guidelines required to be published under the new Regulations will aid firms and provide a degree of certainty in the risk assessment of PEPs. The guidelines are currently in consultation and are expected to be published in final form in June this year.

Risk assessments

4MLD and the Regulations impose an obligation on PE managers to conduct risk assessments on the risks of money laundering and terrorist financing. Written records of these assessments must be maintained and kept up to date. This represents a new requirement and departure from the 2007 Regulations and 3MLD. The risk assessment will need to take account of the business of the manager, its customers, products and services and transactions and the countries in which it operates. The expectation is that these arrangements and written assessments will need to be updated annually and. although they are subject to a proportionality obligation, they will be likely to impose a material burden on compliance departments and on firms' senior management.

What else is changing?

In other ways, the key areas of change under the new regime set down in the Regulations should not involve a substantial overhaul for well-run private equity managers who are already mindful of their AML/CFT obligations. The table below identifies key points of difference between the current requirements and the new Regulations. Many of these provisions should not unduly burden most private equity managers, whilst clearly strengthening the current regime.

	Key changes under the new Regulations
Scope	• The definition of "criminal activity" is expanded to include "tax crimes" in respect of both direct and indirect taxes as defined by the laws of Member States. This broad definition is an attempt to ensure that Member States' AML and CTF legislation is brought into line with the policy of FATF. • 4MLD has expanded the types of firms within its scope. However private equity managers regulated by the FCA are already caught by the 2007 Regulations and will continue to be subject to the new Regulations so it seems unlikely there will be any material impact here for the wider PE industry.
Black listed countries	• 4MLD's policy towards third-country jurisdictions marks a notable departure from 3MLD. 3MLD looked to create a list of countries on a "white-list" which had achieved positive equivalence with the AML and CTF legislation in force in the EU. By contrast, 4MLD seeks to identify and "black-list" those countries which have "strategic deficiencies" in their national AML and CTF regimes and which therefore pose a significant threat to the financial system of the EU ("Black-List Countries"). • Where a PE manager is dealing with a person or firm in a Black-Listed Country, enhanced due diligence measures are to be applied.
Group wide policies	• Firms within scope of 4MLD which are also parent undertakings are obliged to implement group-wide money laundering policies and procedures which is a significant departure from 3MLD. This obligation applies regardless of where a firm's subsidiaries are located.
Simplified due diligence	• There will no longer be a prescribed list of entities which are automatically subject to simplified due diligence ("SDD"). • In accordance with the risk-based approach, firms will need to determine the level of risk posed by each individual customer before applying SDD measures.
Record keeping	• As under the current 2007 Regulations, firms will be required to retain client information for five years after the end of the business relationship. However, under the Regulations, retention periods are different (and potentially shorter) for firms which are being relied upon by another firm to conduct customer due diligence. This creates a risk of discrepancy and is somewhat unsatisfactory for the firm which will continue to be subject to (and liable for) the longer retention period.

The future of UK AML/CFT regulation

Despite not having reached the implementation deadline for 4MLD, following the terrorist attacks in the EU and the leak of the "Panama Papers", further changes to the AML/CFT regime have been proposed in the form of the Fifth Money Laundering Directive ("5MLD"). The intention is to ensure the rules can evolve swiftly in response to ever changing money laundering threats. However, the draft 5MLD is yet to be finalised and published in the Official Journal. Member States are not obliged to implement its provisions alongside 4MLD.

It is difficult to predict whether further changes will be made by the UK in the post-Brexit landscape once the exit process has concluded, but for the time being, UK AML/CFT regulation will continue to be driven by EU standards, in conjunction with the international FATF principles. Anyone expecting a bonfire of regulation in this area following the Brexit vote is likely, at least for the time being, to be disappointed.

11.

BVCA Jargon Buster

Michael Johnson, BVCA
Sundip Jadeja, BVCA
Chris Elphick, BVCA

11. BVCA Jargon Buster

The BVCA works across a wide range of areas and engages with a number of government departments and international bodies from across the world. We are conscious that many acronyms are used and for the benefit of our members, some of these are explained below.

Michael Johnson
BVCA

Sundip Jadeja
BVCA

Chris Elphick
BVCA

UK Government Bodies	
HMT	**HM Treasury** HMT is the government's economic and finance ministry. It is responsible for a number of policy areas that impact the private equity and venture capital industry, including financial regulation and taxation.
HMRC	**HM Revenue & Customs** HMRC is a non-ministerial department of the UK Government responsible for the collection of taxes, the payment of some forms of state support, and the administration of other regulatory regimes.
BEIS	**Department for Business, Energy and Industrial Strategy** BEIS is the government ministry responsible for business, industrial strategy, science, innovation, energy and climate change policy. The BVCA has worked with BEIS and its predecessor, BIS, on a number of areas, including company law, corporate governance, cutting red tape and the register of people with significant control.
DExEU	**Department for Exiting the European Union** DExEU is responsible for coordinating and overseeing the UK's negotiations for leaving the European Union.
FCA	**Financial Conduct Authority** The FCA is the conduct regulator for the financial services industry in the UK, and the prudential regulator for those parts of the sector that are not regulated by the Prudential Regulation Authority, including private equity and venture capital.
PRA	**Prudential Regulation Authority** The PRA is part of the Bank of England. It is the prudential regulator for banks, building societies, credit unions, insurers and major investment firms.
FPC	**Financial Policy Committee** The FPC is part of the Bank of England responsible for identifying and monitoring systemic risks to the UK financial system, including levels of leverage and debt. It can make recommendations to the FCA and PRA to introduce changes to mitigate risks to the financial system.
FRC	**Financial Reporting Council** The FRC is the UK's independent regulator for promoting high quality corporate governance and reporting. The FRC sets standards for corporate reporting and audit practice and monitors and enforces accounting and auditing standards. It also oversees the regulatory activities of the professional accountancy bodies.

The European Union	
European Council	The European Council consists of the heads of government of the 28 EU Member States. It sets the general political direction of the EU and establishes its priorities by adopting “conclusions” following quarterly summits. It is not one of the EU’s legislating bodies, and should not be confused with the Council of the European Union (see below).
European Commission	The European Commission is the executive branch of the European Union. It has the sole power to initiate legislative proposals, which must be approved by both the European Parliament and the Council of the European Union (see below). While the Commission does not have the power to introduce or veto amendments to legislation, if it objects to amendments unanimity is required in the Council for the amendments to be adopted. This, along with the Commission’s agenda setting power, makes it a key player in negotiations over EU laws.
Council of the European Union	The Council of the European Union is one of the European Union’s two ‘co-legislators’, along with the European Parliament (see below). It consists of government Ministers from the EU Member States who meet to discuss, amend and adopt laws proposed by the European Commission (see above).
European Parliament	The European Parliament is, along with the Council of the European Union, one the EU’s co-legislators. It is composed of 751 elected MEPs organised into 8 recognised political groupings. The Parliament can approve and amend proposals made by the Commission, but must agree a final text with the Council in order for a proposal to become law.
Trialogue	Trialogues are informal meetings of representatives from the European Parliament, the Council of the European Union and the European Commission. They are used to agree amendments to legislation that are acceptable to all three parties.
ESAs	**European Supervisory Authorities** The European Banking Authority (“EBA”), the European Insurance and Occupational Pensions Authority (“EIOPA”), and the European Securities and Markets Authority (“ESMA”) are the three European Supervisory Authorities. While national supervisory authorities remain in charge of supervising individual financial institutions, the ESAs aim to improve the functioning of the internal market by promoting harmonised European regulation and supervision by developing Level 2 regulation (secondary legislation) and guidance. They are accountable to the European Parliament and the Council of the European Union.
ESMA	**European Securities and Markets Authority** ESMA, based in Paris, is the ESA (see above) responsible for promoting stable and orderly financial markets. ESMA’s remit includes markets and securities regulation, asset management and investor protection.
EIOPA	**European Insurance and Occupational Pensions Authority** EIOPA, based in Frankfurt, is the ESA (see above) responsible for the supervision of the insurance and pension sectors, and ensuing that policyholders are sufficiently protected.

EBA	**European Banking Authority** The EBA, based in London, is the ESA (see above) responsible for the banking sector. Its overall objectives are to maintain the EU's financial stability and to safeguard the integrity, efficiency and orderly functioning of the banking sector.
RTS	**Regulatory Technical Standards** Level 1 (primary) legislation may empower the Commission to adopt technical standards in the form of RTS. The RTS are prepared by the relevant ESAs, and submitted to the Commission, which has 3 months to adopt the RTS or send them back to the ESAs for amendment. Once adopted by the Commission, there is a 1 month window (which may be extended to 3 months) for the European Parliament and the Council to object to the proposals.
ITS	**Implementing Technical Standards** Level 1 (primary) legislation may empower the Commission to adopt technical standards in the form of ITS. The ITS are prepared by the relevant ESAs, and submitted to the Commission, which has 3 months to adopt the RTS or send them back to the ESAs for amendment. Unlike RTS (see above), ITS are not scrutinised by the Parliament or the Council.
ECB	**European Central Bank** The ECB is the central bank for the Eurozone. It is responsible for monetary policy in the Eurozone, as well as identifying and monitoring systemic threats to financial stability such as excessive levels of leverage and debt.
EIB	**European Investment Bank** The EIB is the EU's development bank, owned by the Member States. It uses its creditworthiness to borrow at low rates on international capital markets and works closely with other EU institutions to finance projects that contribute to EU policy objectives.
EIF	**European Investment Fund** The EIF is a specialist provider of risk finance to SMEs across Europe. Between 2011 and 2015 the EIF invested €2.3bn into UK venture capital and growth funds. It is majority owned by the EIB (see above).

The European Private Equity and Venture Capital Industry	
AFIC	**L'Association Française Des Investisseurs Pour La Croissance** AFIC is the French private equity and venture capital trade association.
BVK	**Bundesverband Deutscher** The BVK is the German private equity and venture capital trade association.
Invest Europe	**Invest Europe** Invest Europe, formerly EVCA, is the pan-European trade body for private equity and venture capital.

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PAE	**Public Affairs Executive** The PAE is the industry's strategic decision-making body for EU-level public affairs. It consists of representatives from the venture capital, mid-market and large buyout parts of the private equity industry, as well as institutional investors and representatives of national private equity associations, including the BVCA. The PAE makes policy submissions on behalf of the European private equity and venture capital industry to the European Institutions and international bodies.
PSC	**Professional Standards Committee** The PSC is the Invest Europe Committee that helps to ensure that proper professional standards are maintained across the European private equity and venture capital industry through its member firms' support of an industry-led Code of Conduct.
Rep Group	**European Representative Group** The Rep Group consists of Invest Europe and the private equity and venture capital associations from individual EU Member States, including the BVCA. It provides a forum for coordinating action at a Member State level and feeds into the work of the PAE (see above).
TLRC	**Tax Legal and Regulatory Committee** The TLRC is the Invest Europe Committee that deals with tax, legal and regulatory matters affecting the European private equity and venture capital industry. The TLRC provides expert advice to the PAE, of which its chair is a member, and drafts position papers and consultation responses for approval by the PAE.

International	
IOSCO	**International Organization of Securities Commissions** IOSCO the international body that brings together national securities regulators, and develops, implements and promotes adherence to international standards for securities regulation. The FCA (see above) is the UK member. It works closely with the G20 and the FSB (see below) on the international regulatory agenda.
FSB	**Financial Stability Board** The FSB is the international body responsible for promoting financial stability. It identifies and monitors global systemic risks, and works with national authorities and international standard setting bodies to respond to threats as they arise. The FSB is chaired by Bank of England Governor, Mark Carney.
OECD	**Organisation for Economic Co-operation and Development** The OECD is an intergovernmental economic organisation designed to promote policies that will improve economic and social well-being. It has a wide-ranging remit including trade and investment, economic growth, employment, health, education and tax. The OECD is responsible for the Base Erosion and Profit Shifting (BEPS) initiative which looks to tackle tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations.

G20	The G20 is the central forum for international cooperation on financial and economic issues made up of 19 countries and the European Union. Much of the global tax transparency agenda and post-financial crisis regulatory framework originated in discussions between finance ministers, central bankers and heads of government at a G20 level.
FATF	**Financial Action Task Force** FATF is an inter-governmental body established to set global standards for combating money laundering, terrorist financing and related threats to the integrity of the international financial system. FATF also monitors the progress of its members in implementing the measures it recommends.

Other Trade Associations and Industry Bodies	
ABI	**Association of British Insurers** The ABI is the trade body for the insurance industry and providers of savings products and services.
AIC	**Association of Investment Companies** The AIC represents the mutual funds industry as well as some venture capital trusts.
AIMA	**Alternative Investment Management Association** AIMA is the global trade associations for the hedge fund and private debt fund industry.
AFME	**Association for Financial Markets in Europe** AFME is the trade body for participants in wholesale financial markets. Primarily leading European and global investment banks as well as other significant capital market players.
BBA	**British Bankers' Association** The BBA is the trade association for the UK banking sector.
EFAMA	**European Fund and Asset Management Association** EFAMA is the trade association for the traditional European investment management industry.
IA	**The Investment Association** The Investment Association is the trade body that represents the UK's traditional investment management industry.
ILPA	**Institutional Limited Partners Association** ILPA is the global industry association for private equity Limited Partners. It aims to promote best practice in the private equity industry, and publishes standardised industry documents and reporting templates.

JMLSG	**Joint Money Laundering Steering Group** The Joint Money Laundering Steering Group is made up of the leading UK trade associations in the financial services Industry. Its aim is to promulgate good practice in countering money laundering and to give practical assistance in interpreting the UK Money Laundering Regulations. This is primarily achieved by the publication of industry-specific guidance.
OTS	**Office for Tax Simplification** The OTS is an independent office of HM Treasury and gives independent advice to the government on simplifying the UK tax system.
PERG	**Private Equity Reporting Group** The PERG is the independent body that monitors conformity with the Walker Guidelines on transparency and disclosure within UK private equity industry.PERG also makes recommendations to the BVCA on improvements in the levels of openness and communication amongst the largest private equity houses in the UK.
WMA	**Wealth Management Association** The WMA is the UK trade association for wealth managers, private banks and stockbrokers.

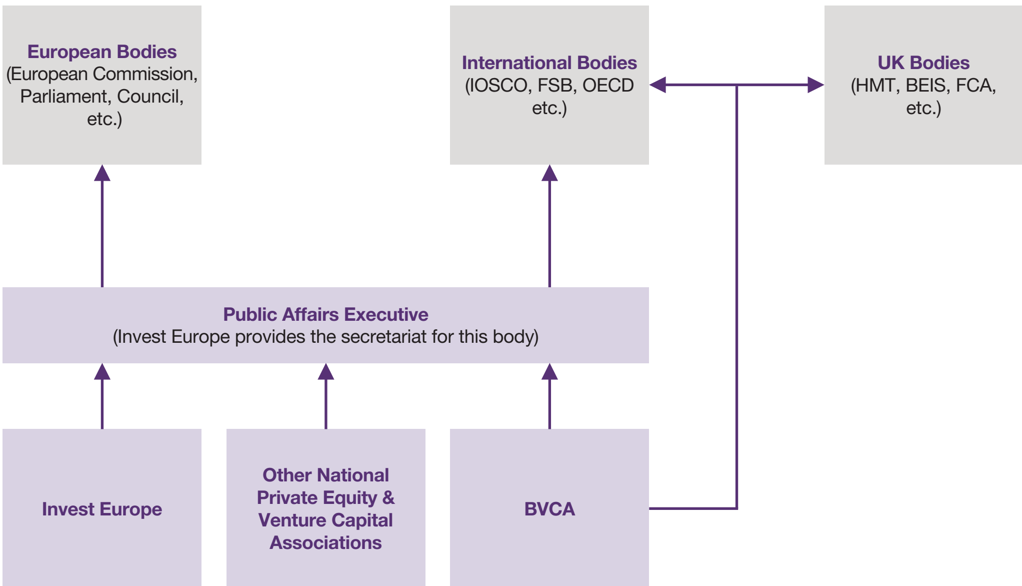
US regulation	
Investment Adviser	**Investment Adviser** Any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities (Section 202(a)(11), Investment Advisers Act of 1940).
RIA	**Registered Investment Adviser** An investment adviser that is registered under the Investment Advisers Act with the SEC (see below) and/or state securities authorities, as applicable.
ERA	**Exempt Reporting Advisor** An investment adviser exempt from registration with the SEC due to falling within the Venture Capital Fund, Foreign Private Adviser or Private Fund Adviser exemptions, among others.
FATCA	**Foreign Account Tax Compliance Act** FATCA is a 2010 United States federal law to enforce the requirement for United States persons including those living outside the U.S. to file yearly reports on their non-U.S. financial accounts to the Financial Crimes Enforcement Network (“FINCEN”).
SEC	**Securities and Exchange Commission** The SEC is an independent government body in the US, and its aim is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

How the BVCA influences policy

The diagram below maps how the BVCA works with its European partners to influence the domestic and international tax, legal and regulatory agenda.

The private equity industry's primary decision-making body for political engagement at a European level is the Public Affairs Executive (PAE), which brings together practitioners from across Europe, representatives from national venture capital associations and Invest Europe—the pan-European industry body. The BVCA, AFIC (the French trade association) and the BVK (the German trade association) have permanent seats on the PAE, and Invest Europe provides the secretariat. Other national trade associations have a rotating seat filled by the country holding the EU presidency, and also feed into decision making through the European Representative Group—a deliberating body composed of representatives of all the national private equity and venture capital associations and Invest Europe.

The BVCA engages directly with policy makers in the UK and international bodies outside of the European Union. However, our close relationship with our colleagues in Europe ensures that our positions are joined up, and the European industry speaks with a unified voice.



12.

BVCA Website

Chris Elphick, BVCA

12. BVCA Website

Chris Elphick
BVCA

The new BVCA website went live in January 2017 and includes a range of new and updated features that make it easier for members to access information about BVCA events, training and policy work.

The website has a dedicated section on tax, legal and regulatory matters covering standardised documents. All our policy submissions can be found in one place with an improved search function, and the matters on our agenda section contains relevant submissions regarding ongoing legislation such as AIFMD, BEPS and the PSC Register.

The BVCA has recently published the second edition of the Brexit Bulletin, a monthly briefing on key policy and political matters including publications on market access and the government's white papers. The Brexit Primer includes information on the upcoming negotiation, relevant legislative developments in the UK, and the institutions that will be involved. Further details on the BVCA's priorities, political analysis and representations can be found on the Brexit portal.

For training and events, there is an all new events and training calendar, an expanded case study section, enhanced filtering functionality for press releases (and more), greater social media integration and an improved section explaining private equity and venture capital. The member directory has been completely overhauled and we have relaunched the annual investor meeting calendar, for LP and GP members to plan their schedules and avoid diary conflicts. Information about all upcoming BVCA events can be found on our calendar.

Further details on the BVCA Council and our committees can be found on the BVCA Governance page, as well as information about our team, and the BVCA Chairmanship.

**British Private Equity &
Venture Capital Association (BVCA)**

5th Floor East, Chancery House
53-64 Chancery Lane
London WC2A 1QS

T. +44 (0)20 7492 0400
E. bvca@bvca.co.uk

www.bvca.co.uk